Supreme Court, U.S.
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No. 95-372 SEP 5 - 1995

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IN THE SUPREME COURT OF THE UNITED STATES

October Term 1995

NORMAN W. SWANSON, *et al.*,
Class A Petitioners, and

CHARLES L. BERRY, *et al.*,
Class B Petitioners,

V.

JANICE H. FAULKNER, *et al.*,
Respondents.

On Petition for Writ of Certiorari to the
United States Court of Appeals for the Fourth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the Full Faith and Credit Act, 28 U.S.C. § 1738, requires a federal district court to give preclusive effect to a state court decision dismissing Plaintiffs' Complaint based upon procedural requirements of a state law remedy previously held inadequate by the district court in determining its own jurisdiction?

PARTIES TO THE PROCEEDING

The Petitioners are: 394 named Class A Petitioner Plaintiffs and approximately 93,455 certified class members who paid state income taxes on their federal pensions; and, seven named Class B Petitioner Plaintiffs and approximately 49,479 certified class members, who are federal active duty and reserve military personnel, who paid state income taxes on their military compensation. The Respondents are: the Secretary of the North Carolina Department of Revenue, the Department of Revenue and the Treasurer of the State of North Carolina. (A list of named Petitioners and Respondents appears in App. F).

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In The
Supreme Court of the United States
October Term, 1995

NORMAN W. SWANSON, *et al.*,
Class A Petitioners, and

CHARLES L. BERRY, *et al.*,
Class B Petitioners,

v.

JANICE H. FAULKNER, *et al.*,
Respondents.

Petition for a Writ of Certiorari to the
United States Court of Appeals for the Fourth Circuit

PETITION FOR A WRIT OF CERTIORARI

Petitioners Classes A and B, as certified by the trial court, hereby petition this Court for Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit.

OPINIONS BELOW

The district court's order, dated May 6, 1994, granted summary judgment in favor of defendants, denied plaintiffs' motion for partial summary judgment, and ordered dismissal of plaintiffs' claims. (App. C). On June 28, 1994, the district court

entered an order on plaintiffs' motion for reconsideration. (App. B). The opinion of the United States Court of Appeals for the Fourth Circuit denying plaintiffs' appeal was entered June 5, 1995. (App. A).

JURISDICTION

On appeal from the United States District Court for the Eastern District of North Carolina, the United States Court of Appeals issued its opinion denying plaintiffs' appeal on June 5, 1995. (App. A). This petition is, accordingly, filed within the time allowed by law. Supreme Court Rule 13.1. Jurisdiction is invoked pursuant to 28 U.S.C. § 1254.

CONSTITUTIONAL AND STATUTORY PROVISIONS

The **Due Process Clause** of the United States Constitution, Amendment XIV, § 1, provides in relevant part:

> [N]or shall any State deprive any person of life, liberty, or property, without due process of law . . .

Title **28 U.S.C. § 1738** provides in relevant part:

> Such Acts, records and judicial proceedings or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken.

Title **28 U.S.C. § 1341** provides:

> The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.

Title **42 U.S.C. § 1983** provides:

> Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory or the District of Columbia, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress.

North Carolina General Statute **§ 105-267**. (App. G).

North Carolina General Statute **§ 105-266.1**. (App. G).

STATEMENT OF THE CASE

This Court issued its opinion in *Davis v. Michigan Department of Treasury*, 489 U.S. 803 (1989) on 28 March 1989, holding Michigan's tax discrimination against federal retirees unconstitutional. On 14 April 1989, Plaintiffs filed this action in the United States District Court for the Eastern District of North Carolina before payment of their 1988 state income taxes were due. The state law remedy, N.C. Gen. Stat. § 105-

267 ("Section 105-267") was alleged to be unclear, uncertain and inadequate. On 16 August 1990, the district court made findings of fact and conclusions of law and rendered a decision that North Carolina's statutory refund remedy was neither plain, speedy, efficient, adequate nor complete, was incapable of being enforced and administered uniformly by Defendants, and was otherwise inadequate. Based upon these findings and conclusions, the district court denied Defendants' motion to dismiss which relied upon the Tax Injunction Act, 28 U.S.C. § 1341, and federal principles of comity. As a result, the district court's jurisdiction over the subject matter of this action and the parties was firmly established. (App. D).

Thereafter, in a state court action, the state trial court entered judgment for these Plaintiffs for full refunds. Defendants appealed the state trial court decision to the Supreme Court of North Carolina. On 6 December 1991 the state supreme court reversed its trial court, denied refunds on the grounds that only prospective relief was available, and dismissed the action. *Swanson v. State of North Carolina*, 329 N.C. 576, 407 S.E.2d 791 (1991).

Plaintiffs petitioned for a Writ of *Certiorari* from the United States Supreme Court. Shortly after this Court's decision in *Harper v. Virginia Dept. of Taxation*, 113 S.Ct. 2510 (1993), the Petition for Writ of *Certiorari* to the North Carolina Supreme Court was granted, dismissal of Plaintiffs' action was reversed, and the case was remanded to the state court for reconsideration in light of *Harper*. *Swanson v. North Carolina*, 113 S.Ct. 3025 (1993).

On remand, the decision of the federal district court that the state remedy was inadequate was considered by the state supreme court. (App. E) Plaintiffs also asked the federal

district court to enter final judgment in light of *Harper* by granting Plaintiffs' request for an order requiring the Defendants to "create in hindsight a nondiscriminatory scheme." (App. C).

After a hearing in federal district court, but before that court had issued further rulings on the issues before it, the state supreme court by split decision applied state, instead of federal, preclusion law and ruled that the federal court decision that the state law remedy was inadequate was not binding. The state supreme court then ruled that the procedural requirements of the state law remedy (the same procedural requirements which made the state law remedy inadequate in the view of the federal district court) required dismissal of Plaintiffs' claims. (App. E). Shortly thereafter the federal district court ruled that it was bound by the state court ruling under principles of federalism and comity, even though that ruling was contrary to the findings of fact and conclusions of law made by the district court some three years earlier. (App. B and C).

The Fourth Circuit affirmed relying almost exclusively on this Court's decision in *Parsons Steel, Inc. v. First Alabama Bank*, 106 S.Ct. 768 (1986). (App. A).

The result is that North Carolina's pre-*Davis* tax scheme remains "in hindsight" discriminatory. The result is *no* relief for over 90,000 federal retirees and almost 50,000 federal active duty and reserve military personnel. The result is no explanation as to how Section 105-267 provides the "plain, speedy, efficient, adequate and complete" remedy the district court below found lacking or as to how it is anything other than a "sham procedure . . . futile from the outset" (App.E, p. 69) which has allowed the state to "pick [its] taxpayer[s'] pocket[s]" and keep "the money when it [was] caught doing so." *Swanson v. State*, 407 S.E.2d 791, 797 (N.C. 1991).

REASONS FOR GRANTING THE PETITION

1. This case presents a significant and novel issue regarding federal court power when confronted with inadequate state law remedies and admitted unconstitutional tax discrimination. Review by this Court is necessary to establish that a state court decision preordained by the inadequacy of a state law remedy cannot oust previously acquired federal jurisdiction. Further, review is required to establish that the Full Faith and Credit Act and this Court's decision in *Parsons Steel, Inc. v. First Alabama Bank*, 106 S.Ct. 768 (1986) do not empower state courts to overrule previously entered federal court orders.

This Court has long afforded states wide latitude in tax matters and has avoided interfering whenever adequate state law remedies were available to aggrieved taxpayers. *National Private Truck Council, Inc. v. Oklahoma Tax Commission*, 115 S.Ct. 2351 (1995) recently reaffirmed this federal policy of noninterference. This case provides the Court an opportunity to give guidance on federal court power when a state's remedies *are found inadequate*.

Here, the federal district court below found North Carolina's state law remedy for challenging an admittedly unconstitutional tax inadequate as applied to Plaintiffs and assumed jurisdiction over Plaintiffs' claims pursuant to 42 U.S.C. § 1983 ("Section 1983"). On August 16, 1990, the district court below decided that Section 105-267 as interpreted and applied to plaintiffs was neither plain, speedy, efficient, adequate, nor complete. (App. D, pp. 36-37). The court made these findings in response to defendants' motion to dismiss and, in the process, considered extensive and voluminous evidence. The evidence presented showed, *inter alia*, that: (a) Defendants could not administer

Section 105-267 (App. D, p. 35); (b) Defendants had no authority to provide relief to Plaintiffs under Section 105-267 and therefore its demand requirement was futile, *Coca-Cola v. Coble*, 238 S.E.2d 780 (N.C. 1977); (c) Defendants misled Plaintiffs as to when requests for refunds were due by expressly advising them that they had three years to request refunds and never correcting this advice until it was too late (App. D. pp. 34); and (d) Defendants used previously unannounced form and content requirements to reject Plaintiffs' class demands after it was too late to conform the demands to the newly-imposed requirements. (App. D, pp. 34-35).

After the federal court assumed jurisdiction and determined that the state law remedy was inadequate, Plaintiffs pursued a state court action offering the state an opportunity to decide for itself how to correct the inadequacies of the state law remedy. Despite the earlier federal court order, the state appellate court declined to acknowledge the inadequacy of the state law remedy and applied it to dismiss Plaintiffs' claims. (App. E). Defendants then obtained summary judgment dismissal in this federal action based upon the final judgment which resulted from the state court applying the inadequate state law remedy. (App. B and C).

Plaintiffs appealed. The appelate court below affirmed on the basis of the Full Faith and Credit Act and this Court's decision in *Parsons Steel, Inc. v. First Alabama Bank*, 106 S.Ct. 768 (1986). In doing so, that court rejected plaintiffs' argument that once federal jurisdiction was established over plaintiffs' Section 1983 claims, this Court's decisions in *Harper v. Virginia Dep't of Taxation*, 113 S.Ct. 2510 (1993) and *McKesson v. Division of Alcholic Beverages and Tobacco*, 110 S.Ct. 2238 (1990) mandated "meaningful backward looking relief" to these plaintiffs which "creates in hindsight a nondiscriminatory

scheme" and this Court's decision in *Felder v. Casey*, 108 S.Ct. 2302 (1988) mandated such relief without regard to state law procedural hurdles.[1] The entire discussion by the Court below of plaintiffs' reliance on *Harper*, *McKesson* and *Felder* consisted of:

> "We also reject plaintiffs' alternative argument, citing *Felder v. Casey*, 487 U.S. 131, 138 (1988), that the Supremacy Clause bars the application of § 267 because it "conflicts in both its purpose and effects with the remedial objectives of § 1983." *Felder* reversed a Wisconsin Supreme Court decision that applied the time limitation of a state notice-of-claim statute to § 1983 actions. Here, it is not the § 1983 action that was barred by the § 267 time limitation, but state administrative relief."

Otherwise, the court below based its ruling as to Class A and Class B Petitioners entirely upon *Parsons Steel* and effectively held that the Full Faith and Credit Act policies inherent in that decision override the federal interest in providing a forum for vindication of federal constitutional rights in the face of inadequate state law remedies. This latter federal interest was expressed in *Harper*, *McKesson* and *Felder*.

The issue thus presented asks this Court to reconcile the policies of *Harper*, *McKesson* and *Felder* with that of *Parsons Steel*. This question has not been previously addressed by the Court.

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1 Of course, if the federal district court had found the state law remedy adequate, that court would never have reached the *Felder* issue since it would have lacked jurisdiction.

2. Absent review by this Court, the precedent established by the lower appellate court's decision will result in multiplicitous litigation in state and federal courts and will leave unresolved a conflict among the circuits. This Court should anticipate that based upon the Fourth Circuit's decision litigants may attempt to obtain "two bites at the apple" for each issue presented. Consider the summary judgment motion which is denied by a federal district court and subsequently presented to a state court and granted on the same issues and same facts presented by the same parties. Based upon the lower court's reading of *Parsons Steel*, the federal court when presented with the subsequent state court ruling would have little choice but to dismiss the action before it (or at least stay all proceedings pending state court appeals and exhaustion of efforts to obtain review by this Court). Such result would occur even if the state court decision was rendered during the federal court trial.

Other circuits apply preclusion law in similar circumstances differently than did the Fourth Circuit here. In *Freeman United Coal Mining Co. v. OWCP*, 20 F.3d 289 (7th Cir. 1994), the Seventh Circuit addressed the preclusive effect of a state industrial commission decision finding only partial disability on a prior federal administrative law judge's finding of total disability -- which federal decision was still subject to, and was being addressed on, motion for reconsideration. The Court there found no preclusion stating:

> As pointed out by the Director in its brief, however, Freeman faces a more fundamental problem in attempting to assert collateral estoppel in this case. This is because the finding Freeman seeks to estop . . . was rendered three years *before* the decision of the Illinois Industrial Commission. This does appear to be dispositive

> for in such situations "the first judgment can scarcely be faulted for ignoring a second judgment that had not yet been entered." 18 Charles A. Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and Procedure* § 4404 at 30 (1981). The law of collateral estoppel is intended to protect the parties from the burden of relitigating the same issue following a final judgment and to promote judicial economy by preventing needless litigation. That is why it is invoked to prevent, or estop, relitigation of the same issues in a *subsequent* case. But where, as here, the effort has already been undertaken in the case before the ALJ and the decision rendered on the merits, the reasons for collateral estoppel are hardly served.

Id. at 294 (citations omitted).

In *Industrial Systems, Inc. v. Computer Curriculum Corp.*, 35 F.3d 813 (3rd Cir. 1994), the Third Circuit found *Parsons Steel* inapposite in addressing the preclusive effect of a state court interpretation of the Commerce Clause when federal jurisdiction of the subject matter had been established before the state court decision. The court stated:

> "*Parsons Steel, Inc. v. First Alabama Bank*, 474 U.S. 518, 106 S.Ct. 768, 88 L.Ed.2d 877 (1986), which ISI cites, is inapposite. . . . It did not hold, as ISI implicitly suggests, that a state court's consideration of an issue precludes a federal court from doing so.

Id. at 821 n. 14.

The Fifth Circuit in *Cycles, Ltd. v. Navistar Financial Corp.*, 37 F.3d 1088 (5th Cir. 1994) considered a district court decision under nearly identical circumstances to those at issue here except that it involved a subsequent factually inconsistent decision by a different federal district court instead of a state court. In that case, a Mississippi district court after fully litigating the issue of defendant's conversion of plaintiff's property entered a nonappealable order in favor of plaintiff. Subsequently, an Arkansas district court entered an order against the plaintiff which undermined a critical factual premise of the Mississippi court's order. In reversing the Mississippi district court which felt compelled to revise its earlier decision because of the perceived preclusive effect of the subsequent Arkansas decision, the Fifth Circuit reasoned:

> Yet the mark of a decision's maturity for the purposes of issue preclusion is whether the decision was fully litigated. If the first decision had the power to preclude relitigation of the same issues, for our purposes it does not matter if a later case ignores the opinion's preclusive power, as here. In either event, the fully litigated opinion stands unaffected by a later inconsistent judgment.
>
> We and the other circuits have similarly ruled that the preclusive reach of decisions does not extend to prior decisions.

Id. at 1091 (citations omitted).

In *American Postal Workers Union v. United States Postal Service*, 736 F.2d 317 (6th Cir. 1984), the Sixth Circuit Court of Appeals held that the defense of *res judicata* would not lie to

require dismissal of suit by a local union in Columbus, Ohio, even after the Fifth Circuit Court of Appeals upheld the dismissal of a similar suit by a local union in Dallas, Texas where the original decision on a motion to dismiss in the Columbus case was made before the decision on the same issue in the Dallas case. The Court reasoned:

> Moreover, even assuming that there was sufficient identity between the parties, *res judicata* would still not lie because the decision on the motion to dismiss in the Columbus case came *before* the decision on the same issue in the Dallas case.
>
> * * * *
>
> If anything, the Columbus decision should have been given preclusive effect in the Dallas case. Admittedly, there had been no final judgment in the Columbus case, but such a judgment is not required so long as there has been a final decision with respect to the issue to be given preclusive effect (in this case, the motion to dismiss). . . . Once the preclusive effect of the Columbus decision was not recognized in the Dallas case, it would be appropriate to give preclusive effect to the Dallas decision in all subsequent cases,[2] . . . *but not to make it binding*

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[2] The Sixth Circuit here makes reference to the general rule that, once the preclusive effect of a court's decision (whether that decision is rendered in a federal or a state court), has been determined in a later proceeding by another court (whether the subsequent court is a federal or a state court), that decision is binding in all *subsequent* cases unless and until reversed on appeal. *See*

> *in the first case*. Therefore, we find it was error for the trial judge to grant *res judicata* effect to the Dallas decision.

Id. at 319 (emphasis added) (citations omitted).

See Howell v. Thomas, 566 F.2d 469 (5th Cir.) (per curiam), *cert. denied* 439 U.S. 826 (1978) (subsequent proceeding cannot collaterally estop prior proceeding); *Flood v. Harrington*, 532 F.2d 1248 (9th Cir.) (subsequent case does not control outcome of prior case). *See generally, Clark Equipment Company v. United States*, 912 F.2d 113 (6th Cir. 1990), *cert. den.*, 500 U.S. 941, 111 S.Ct. 2236, 114 L.Ed.2d 478; *Masedo v. Honda Motor Co. Ltd.*, 861 F.2d 1248 (11th Cir. 1988); *Kaempfer v. Brown*, 684 F.Supp. 31 (D.D.C. 1988); *aff'd*, 872 F.2d 496 (D.D.C. 1989).

Parsons Steel addressed the preclusion effect of a state court decision in the context of three separate actions: (1) a federal court proceeding which concluded with a judgment for the defense, (2) a subsequent state court judgment for plaintiff and (3) a federal court action to enjoin enforcement of the state court judgment filed after the state court determination. 474 U.S. at 520-521. The Court did not address the dilemma presented here and addressed by the various Circuits in the decisions cited above.

Accordingly, review is necessary to provide guidance to the Circuits as to the preclusive effect of state court decisions

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Migra v. Warren City School District Bd. of Educ., 465 U.S. 75 (1984); *Kremer v. Chemical Construction Corp.*, 456 U.S. 461 (1982); *Allen v. McCurry*, 449 U.S. 90 (1980). It was this general rule which the Court applied in *Parsons Steel*.

rendered during the pendency of federal court actions where the federal court has already assumed jurisdiction of the subject matter and has already rendered a decision inconsistent with the subsequent state court decision.

3. Review by this court is necessary for these Plaintiffs' to have their day in court on the merits of their claim that North Carolina discriminated in its taxation of them. Defendants here have avoided, to this day, a binding judicial decision on plaintiffs' constitutional challenges to the taxes at issue. The North Carolina Supreme Court has determined that the one opportunity to be heard which plaintiffs have received (the summary judgment hearing before the North Carolina Superior Court) was of no force or effect and should never have occurred. The district court's prophecies in August of 1990 about the efficacy of the state court remedy have been proven entirely true. Defendants have made *no meaningful changes* in their procedures for handling constitutional challenges to state taxes since that time. Plainly, no rulings could be more inconsistent than the district court's holding that the Tax Injunction Act standard was not met by the state remedy and the North Carolina Supreme Court's ruling that the Due Process standard was met by the very same remedy on the very same facts.

A plain, speedy, and efficient remedy under the Tax Injunction Act, 28 U.S.C. § 1341, is one that provides a taxpayer with a *full hearing* and judicial determination at which he or she may raise any and all constitutional objections. *Rosewell v. LaSalle National Bank*, 450 U.S. 503, 513 (1981). Similarly, among the fundamental requirements of Due Process is the opportunity to be heard "at a meaningful time and in a meaningful manner." *McKesson v. Division of Alcoholic Beverages and Tobacco*, 496 U.S. 18, 39, n.22 (1990) (quoting

Mathews v. Eldridge, 424 U.S. 319, 333 (1976)). In the context of state taxation where no pre-deprivation remedy exists, the opportunity to be heard at a meaningful time and in a meaningful manner must provide "a fair opportunity to challenge the accuracy and legal validity of [the] tax obligation . . . ." *McKesson*, 496 U.S. at 39.[3] The common denominator between the Tax Injunction Act standard and the Due Process Clause standard is that a taxpayer in each instance must ultimately be provided a full hearing and opportunity to raise any and all constitutional objections to the challenged tax. Therefore, once a state remedy is found to be lacking under the Tax Injunction Act standard (*i.e.*, once a court finds that a taxpayer will not be afforded a full hearing and opportunity to raise any and all constitutional objections to the challenged tax by pursuing the state remedy), it is impossible to conclude that the state remedy provides the taxpayer a fair opportunity to challenge the legal validity of the tax obligation or a hearing at a meaningful time and in a meaningful manner.

The district court ruling came first, almost four years before the North Carolina Supreme Court's ruling. It remains unreversed, unmodified, and as fully accurate today as it was four years ago. Defendants' motion to reconsider the ruling was denied. (App. at B and C). That ruling should be the law of this case. *Stoll v. Gottlieb*, 305 U.S. 165, 170 (1938). Under these circumstances, the August 16, 1990 order foreclosed the Due Process claims in plaintiffs' favor unless and until reversed or modified by the district court or a federal appellate court. No

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[3] Unlike the Tax Injunction Act (which focuses solely upon a taxpayer's opportunity to raise all constitutional objections to the tax), Due Process requires, in addition to the opportunity to challenge the tax obligation, a "clear and certain remedy" in the event the challenge is successful. *McKesson*, 496 U.S. at 39.

subsequent state court decision should change the result or force the district court into the inconsistent rulings which have occurred here.

To succeed in their request for partial summary judgment filed in the court below, plaintiffs need only show that defendants violated their constitutional rights under color of state law. 42 U.S.C. § 1983. As to Class A, defendants concede that taxes were unconstitutionally collected by defendants under authority of the Department of Revenue in contravention of the standards enunciated in *Davis*. Therefore, Class A plaintiffs have satisfied all of the elements necessary to obtain meaningful relief under Section 1983. As to both classes, the district court's August 16, 1990 order established, as the law of this case, that defendants did not afford plaintiffs a full hearing and opportunity to present any and all constitutional challenges to the taxes collected from them. Such a hearing is a necessary requirement of due process.

Because the state court determination using the inadequate state law remedy was given preclusive effect, Plaintiffs here are out of court without a full hearing and opportunity to be heard and without the "meaningful backward looking relief" mandated by this Court. Further, they remain the victims of a taxation scheme which "in hindsight" is discriminatory - the antithesis of this Court's holding in *Harper*. Review by this Court is necessary to correct not only this injustice but also misapplication of this Court's decisions in *Harper*, *McKesson* and *Felder*.

CONCLUSION

Therefore, and for all of the foregoing reasons, Petitioners respectfully request that this Court issue a Writ of *Certiorari* to the United States Court of Appeals for the Fourth Circuit.

Respectfully submitted,

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APPENDIX

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APPENDIX A

PUBLISHED
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

NORMAN W. SWANSON et al.

No. 94-1971

Plaintiffs-Appellants,

v.

JANICE H. FAULKNER, Secretary of the North Carolina Department of Revenue; HARLAN E. BOYLES, Treasurer of the State of North Carolina; NORTH CAROLINA DEPARTMENT OF REVENUE,

Defendants-Appellees.

No. 94-2022

NORMAN W. SWANSON et al.

Plaintiffs-Appellees,

v.

JANICE H. FAULKNER, Secretary of the North Carolina Department of Revenue; HARLAN E. BOYLES, Treasurer of the State of North

Carolina; NORTH CAROLINA
DEPARTMENT OF REVENUE,

Defendants-Appellants.

Appeals from the United States District Court for the Eastern District of North Carolina, at Raleigh. Malcolm J. Howard, District Judge. (CA-89-282-5-H)

Argued: March 6, 1995
Decided: June 5, 1995

Before WILKINSON and WILKINS, Circuit Judges, and SPROUSE, Senior Circuit Judge.

Affirmed by published opinion. Senior Judge Sprouse wrote the opinion, in which Judge Wilkinson and Judge Wilkins joined.

COUNSEL

ARGUED: Robert E. Fields, III, WOMBLE, CARLYLE, SANDRIDGE & RICE, P.L.L.C., Raleigh, North Carolina, for Appellants. Thomas Frederick Moffitt, Special Deputy Attorney General, NORTH CAROLINA DEPARTMENT OF JUSTICE, Raleigh, North Carolina, for Appellees. **ON BRIEF:** G. Eugene Boyce, William C. Raper, Keith W. Vaughan, WOMBLE, CARLYLE, SANDRIDGE & RICE, P.L.L.C., Raleigh, North Carolina; Charles H. Taylor, Winston-Salem, North Carolina, for Appellants. Michael F. Easley, Attorney General of North Carolina, Edwin M. Speas, Jr., Senior Deputy Attorney General, Norma S. Harrell, Special Deputy Attorney General, Marilyn R. Mudge, Assistant Attorney General, NORTH CAROLINA DEPARTMENT OF JUSTICE, Raleigh, North Carolina, for Appellees.

OPINION

SPROUSE, Senior Circuit Judge:

Until 1989, the State of North Carolina fully exempted state pension benefits from taxable income but exempted only the first $3,000 of federal pension benefits. Plaintiffs, retired federal employees[1] who sought refunds for overpayments made under this unconstitutional tax scheme,[2] were denied relief by North Carolina tax authorities on the basis of their failure to comply with the time limitations of a state statute providing for refunds. Plaintiffs then brought this § 1983 class action two weeks after the Supreme Court, in Davis v. Michigan Dep't of Treasury, 489 U.S. 803 (1989), declared unconstitutional the type of taxation employed by North Carolina. In demanding declaratory, injunctive, and monetary relief, they asserted that the time limitations for claiming refunds contained in N.C. Gen. Stat. § 105-267 (1992) ("§ 267") deprived them of their federal constitutional right to due process of law.[3] They now appeal the

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[1] Plaintiffs are divided into two classes. The retired federal employees are termed "Class A plaintiffs." Also joined in this action are North Carolina taxpayers who, in the relevant time frame, were active duty military personnel or reservists ("Class B plaintiffs"). The claims of the Class B plaintiffs will be described in more detail infra note 4.

[2] In Davis v. Michigan Dep't of Treasury, 489 U.S. 803 (1989), the United States Supreme Court ruled unconstitutional a state statute giving state retirement income more favorable tax exemption treatment than federal retirement income. In Harper v. Virginia Dep't of Taxation, 125 L. Ed. 2d 74 (1993), the Supreme Court ruled that Davis applied retroactively.

[3] Section 267 provides, in pertinent part:

Whenever a person shall have a valid defense to the enforcement of

district court's grant of summary judgment against them in favor of North Carolina and its taxing authorities ("the State"). The court ruled that an earlier state court judgment involving the same parties and the same issues precluded it from acting on plaintiffs' claims. Because we believe full faith and credit principles compelled the district court's decision, we affirm.

Until Davis, North Carolina and twenty-two other states taxed state pensioners more favorably than federal pensioners. After Davis, North Carolina promptly revised its tax scheme to comport prospectively with the Supreme Court's holding. In this litigation, the State does not deny that its previous practice violated the Davis principle.[4] Nor do plaintiffs contest North

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> the collection of a tax assessed or charged against him or his property, such person shall pay such tax to the proper officer, and such payment shall be without prejudice to any defense of rights he may have in the premises. At any time within 30 days after payment, the taxpayer may demand a refund of the tax paid in writing from the Secretary of Revenue and if the same shall not be refunded within 90 days thereafter, may sue the Secretary of Revenue in the courts of the State for the amount so demanded. Such suit may be brought [in state court] . . . at any time within three years after the expiration of the 90-day period allowed for making the refund. If upon the trial it shall be determined that such a tax or any part thereof was levied or assessed for an illegal or unauthorized purpose, or was for any reason invalid or excessive, judgment shall be rendered therefor, with interest . . .
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> N.C. Gen. Stat. § 105-267 (1992).

[4] The State concedes its prior tax scheme violated the constitutional rights of Class A plaintiffs, but argues Class B plaintiffs were not so affected. While taxation of Class A plaintiffs is indistinguishable from that of the prevailing Davis plaintiffs, Class B plaintiffs cite Davis only by analogy. They claim that the State's former practice of granting a $1,500 annual income tax exclusion to members of the North Carolina National Guard while providing no exclusion for active duty military personnel and reservists unconstitutionally

Carolina's current income tax system. Instead, the present dispute focuses on the State's procedure by which taxpayers may obtain refunds for excessive payments under the prior tax system. Under North Carolina General Statute § 267, supra note 3, the taxpayer must first pay the assessed tax and then file a written demand for refund with the Secretary of Revenue within thirty days. If the Secretary fails to issue a refund within ninety days, § 267 provides that the taxpayer may bring a refund action in state court within three years of the end of the ninety-day period. This is the sole resort for a taxpayer seeking to challenge the legality of a state tax. By contrast, the immediately preceding section of the state tax code, § 266.1,[5] provides the avenue for recovering an excessive amount paid because of a clerical or mathematical error and does not contain the initial thirty-day

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favored income derived from a state source over that derived from a federal source (members of the North Carolina National Guard are compensated primarily by the federal government, but receive a small portion of their pay from the state). While we express no opinion as to the merits of this dispute, we will assume arguendo that Class B plaintiffs were unconstitutionally taxed. Therefore, we may consider the two classes of plaintiffs as one for purposes of this appeal.

[5] In pertinent part, § 266.1 provides:

> (a) Any taxpayer may apply to the Secretary of Revenue for refund of tax or additional tax paid by him at any time within three years after the date set by the statute for filing of the return or application for a license or within six months from the date of payment of such tax or additional tax, whichever is later. The Secretary shall grant a hearing thereon, and if upon such hearing he shall determine that the tax is excessive or incorrect, he shall resettle the same according to the law and the facts, and adjust the computation of tax accordingly.

N.C. Gen. Stat. § 105-266.1 (1992).

limitation period. Coca-Cola Co. v. Coble, 238 S.E.2d 780, 782-83 (N.C. 1977). So, it is clear under North Carolina law that under § 267 a refund demand must be made within thirty days after paying the illegal tax. It is equally clear that under § 266.1 a taxpayer can apply for a refund within three years of the tax return deadline if the erroneous assessment was due to a clerical or mathematical error -- unhindered by the thirty-day requirement.

Plaintiffs contend that the State published tax bulletins and instruction booklets informing them that any request for refund could be filed within three years. They could not discern, they claim, that this information related only to filings under § 266.1 because the State's publications simply ignored § 267. The plaintiffs emphasize that the State did not publicize the existence of § 267 until four days before the filing deadline for the 1988 tax year (approximately two weeks after Davis). By this time, more than thirty days had passed from the time many plaintiffs had filed their tax returns. As a consequence, the thirty-day demand requirement of § 267 barred them from receiving refunds.

In their federal complaint, plaintiffs requested full and immediate refunds for all overpayments. They essentially argue that the State's application of § 267, particularly in light of the misinformation provided them, violated their constitutional right to due process of law. Here, as in the court below, the State asserts that all plaintiffs' claims are barred by the Eleventh Amendment, the federal Tax Injunction Act, principles of comity, and plaintiffs' failure to comply with § 267.

In an order filed in August of 1990, the district court denied the State's motion to dismiss. The court held it had jurisdiction

despite the Tax Injunction Act and principles of comity[6] because the state remedy was not "plain, speedy, and efficient." It retained the declaratory and injunctive portions of the action but held that the Eleventh Amendment barred plaintiffs' claims for monetary relief.

After an appeal to this court unrelated to the matters before us now, plaintiffs' federal action remained dormant while they pursued a refund action in the North Carolina courts. The North Carolina Supreme Court initially dismissed plaintiffs' claims, holding Davis did not apply retroactively. Swanson v. North Carolina ("Swanson I"), 407 S.E.2d 791 (N.C.), adhered to on reh'g, Swanson v. North Carolina ("Swanson II"), 410 S.E.2d 490 (N.C. 1991). The United States Supreme Court vacated and remanded in light of Harper v. Virginia Dep't of Taxation, 125 L. Ed. 2d 74 (1993), which held Davis applies retroactively.

At this point, plaintiffs sought to resuscitate their federal action, moving for an entry of final judgment enjoining defendants "from further denial of refunds to plaintiffs." The State responded by asking the district court to deny the motion and to hold that the Eleventh Amendment barred even declaratory or injunctive relief. The State also moved the court to reconsider its 1990 Tax Injunction Act ruling. Ultimately, both parties moved for summary judgment.

While these motions were pending in federal court, the North Carolina Supreme Court upheld the State's application of§ 267 and denied plaintiffs' requested refunds. In reversing the state trial court's grant of summary judgment in plaintiffs' favor, it

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[6] The court treated the Tax Injunction Act as essentially codifying principles of comity in this area, an interpretation neither party disputes.

ruled that § 267 satisfied due process. Swanson v. North Carolina ("Swanson III"), 441 S.E.2d 537 (N.C.), cert. denied, 130 L. Ed. 2d 598 (1994). Swanson III also rejected plaintiffs' argument that the federal district court's 1990 Tax Injunction Act order should have precluded the state court's holding concerning due process. The state supreme court reached this decision by concluding that the federal order had no preclusive effect because it was not "final."

After the North Carolina Supreme Court ruling, the district court entered summary judgment in favor of the State on the plaintiffs' federal claims. It held that Swanson III's due process ruling precluded a different result in federal court. The district court, however, denied both the State's motion to dismiss based on the Eleventh Amendment and its motion to reconsider the court's Tax Injunction Act ruling. Plaintiffs then moved for reconsideration, contending sequentially that the court misapplied the doctrine of issue preclusion, that the Eleventh Amendment did not prevent the court from granting relief, and that their noncompliance with § 267 was immaterial because § 267, constituting a state administrative burden upon a federal right, is inapplicable to § 1983 actions. The court denied the motion.

Plaintiffs appeal the district court's final judgment and its denial of their motion to reconsider. The State cross-appeals, citing as error the district court's ruling that plaintiffs' action was not barred by the Eleventh Amendment and its ruling that the Tax Injunction Act did not preclude federal jurisdiction.

In considering the propriety of the district court's grant of summary judgment, we apply de novo review, employing the same standards used by the district court. Temkin v. Frederick County Comm'rs, 945 F.2d 716, 718 (4th Cir. 1991), cert.

denied, 502 U.S. 1095 (1992). Summary judgment is appropriate where "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). The court must resolve all reasonable inferences in favor of the nonmoving party. Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986).

Plaintiffs' appeal essentially rests on their contention that the district court erred in granting summary judgment on the basis of issue preclusion.[7] They assert that the state court should have been precluded from deciding the due process issue in the State's favor because the federal district court had, in effect, already decided the due process issue in their favor when it resolved the federal Tax Injunction Act question in its 1990 order. In plaintiffs' view, the district court's earlier holding that § 267 was not "plain, speedy and efficient" in the Tax Injunction Act context foreclosed the state court's later holding that § 267 was a "clear and certain" remedy as required by due process. Citing McKesson v. Division of Alcoholic Beverages and Tobacco, 496 U.S. 18, 31 (1990), plaintiffs point out that to satisfy due process, the state's remedy must be "clear and certain," so as to "insure that the opportunity to contest the tax is a meaningful one." Id. at 39. The Tax Injunction Act deprives federal district

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[7] In conformity with the modern trend, we use the term "issue preclusion" instead of the older "collateral estoppel." See Robi v. Five Platters Inc., 838 F.2d 318, 321 n.2 (9th Cir. 1988); Carter v. City of Emporia, 815 F.2d 617, 619 n.2 (10th Cir. 1987); Wade v. City of Pittsburgh, 765 F.2d 405, 408 (3d Cir. 1985); 18 C. Wright, A. Miller, & E. Cooper, Federal Practice and Procedure § 4402 (1981). Cf. Kutzik v. Young, 730 F.2d 149, 150 n.* (4th Cir. 1984) (expressing preference for term "claim preclusion" instead of "res judicata").

courts of jurisdiction to hear any case involving state taxation unless the state fails to provide a "plain, speedy and efficient remedy." 28 U.S.C.A. § 1341 (West 1993). In its 1990 order, the district court held that it was not deprived of jurisdiction because the State's misapplication of § 267 rendered the plaintiffs' remedy too"uncertain" to be considered "plain, speedy and efficient." It noted that, by misapplying § 267, the State had "deprived the plaintiffs of a full hearing and judicial determination of their claims."

Emphasizing this district court finding, plaintiffs urge that a putative remedy, such as the one offered by § 267, which fails to meet the "plain, speedy and efficient" standard of the Tax Injunction Act cannot provide them with a meaningful opportunity to litigate their claims as required by the due process clause. They argue that this is particularly true here because the federal court finding of "uncertainty" cannot be reconciled with the state court determination that the same remedy was "clear and certain." The district court, plaintiffs continue, was not obliged to give the state court's Swanson III judgment preclusive effect because the state court failed to give preclusive effect to the district court's 1990 order.

The State of North Carolina stresses on appeal that the North Carolina Supreme Court correctly determined that it was not bound by the 1990 federal court order because that order was not final. It also, of course, counters plaintiffs' argument that the 1990 order effectively decided the due process issue.[8] Finally,

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[8] The finality and identity of issues arguments were extensively briefed by both parties. Both arguments concern the question of whether the North Carolina Supreme Court should have found itself precluded by the 1990 order and the concomitant question of whether that contended failure relieved the federal district court of the obligation to give full faith and credit to the North Carolina Supreme Court's decision on due process. As we note, infra,

it opines that Parsons Steel, Inc. v. First Alabama Bank, 474 U.S. 518 (1986), requires full faith and credit recognition of the North Carolina Supreme Court's decision in Swanson III, even if incorrect.

We certainly agree with the State's reliance on Parsons. In fact, both parties tend to underestimate its force. In Parsons, a state court decided an earlier ruling by a federal district court did not preclude it from reaching the merits. Subsequently the district court declined to give preclusive effect to the state court's preclusion decision, instead judging for itself the preclusive force of its earlier ruling and enjoining the plaintiffs from further prosecuting the state action. The Eleventh Circuit affirmed. The Supreme Court reversed, holding that a state court's decision on preclusion is entitled to the same full faith and credit deference as any other decision. Parsons, 474 U.S. at 525. In our view, a straightforward application of Parsons disposes of plaintiffs' arguments. In Swanson III, the North Carolina Supreme Court considered whether it was precluded by the prior federal court order and decided it was not. The Parsons principle makes this determination, even if erroneous, binding on the federal district court.

Citing American Postal Workers Union v. United States Postal Serv., 736 F.2d 317, 319 (6th Cir. 1984), however, plaintiffs argue that the federal district court has the power to follow its 1990 order and ignore Swanson III because it, in effect, decided the due process issue before the North Carolina state court decided that issue. We are not persuaded. In the first place, the

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Parsons requires that even an erroneous state court ruling concerning preclusion is entitled to full faith and credit. As a result, we do not consider the controversies surrounding the nature of the 1990 order.

Sixth Circuit, in Postal Workers, considered circumstances unlike those here. It weighed and resolved a conflict between rulings of two federal district courts. In our view, however, even if Postal Workers had involved a conflict between a state court and a federal district court, Parsons would have overruled that decision.[9] In a nutshell, Parsons dictates that full faith and credit principles require a federal court to recognize a state court's prior resolution of preclusion issues just as a state court is bound to respect a federal court's prior rulings with respect to preclusion. Under Parsons, if plaintiffs believed that the state court's preclusion ruling was erroneous, their remedy was an appeal to the United States Supreme Court, not an action in the lower federal courts.

The federal district court then was required to give the same preclusive effect to the North Carolina Supreme Court ruling as would the courts of that state. Dionne v. Mayor and City Council of Baltimore, 40 F.3d 677, 682 (4th Cir. 1994) (federal courts apply state preclusion rules to determine whether a prior state court decision has preclusive effect). Left for determination, then, is whether the district court, under North Carolina law, correctly found itself precluded by the state court's Swanson III due process decision. In North Carolina, issue preclusion applies when the following requirements are met:

> (1) The issues to be concluded must be the same as those involved in the prior action; (2) in the prior action, the issues must have been raised and actually litigated; (3) the issues must have been material and relevant to the disposition of the prior action; and (4) the determination made of those issues in the prior action

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[9] Parsons was decided some two years after Postal Workers.

> must have been necessary and essential to the resulting judgment.

Beckwith v. Llewellyn, 391 S.E.2d 189, 191 (N.C. 1990) (quoting King v. Grindstaff, 200 S.E.2d 799, 806 (N.C. 1973)).

We conclude that the district court correctly applied these rules. The issue it found precluded--whether § 267 satisfied the McKesson due process test as a meaningful post-deprivation remedy--was the same as that decided by the North Carolina Supreme Court in Swanson III. Both parties aggressively litigated this in state court. The due process determination was not only material and relevant to the state court judgment, but necessary and essential as well. Indeed, plaintiffs' argument that § 267 fell short of constitutional due process standards comprised the linchpin of their case. We are easily persuaded that the state court decision satisfied all four of North Carolina's requirements for issue preclusion.

We also reject plaintiffs' alternative argument, citing Felder v. Casey, 487 U.S. 131, 138 (1988), that the Supremacy Clause bars the application of § 267 because it "conflicts in both its purpose and effects with the remedial objectives of § 1983." Felder reversed a Wisconsin Supreme Court decision that applied the time limitation of a state notice-of-claim statute to § 1983 actions. Here, it was not the § 1983 action that was barred by the § 267 time limitation, but state administrative relief.

Finally, plaintiffs contend that the district court's final order was overbroad because it ignored those taxpayers who complied with § 267 and still were denied relief. Plaintiffs support this claim with documentation from several taxpayers thus affected. The State responds by admitting that administrative problems have resulted in long delays for some refunds, but adds that

these claims now will be promptly reviewed and appropriate action taken. We are influenced in accepting this assurance by our view that such administrative dalliance does not rise to a constitutional level.

Ruling in favor of the State, we need not reach the issues presented by its cross-appeal. The judgment of the district court is affirmed.

AFFIRMED

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
RALEIGH DIVISION

NO. 89-282-CIV-5-H

NORMAN W. SWANSON, et al.,	)	
	)	
Class A Plaintiffs,	)	
	)	
CHARLES L. BERRY, et al.,	)	
	)	**ORDER**
Class B Plaintiffs,	)	[Filed 6/28/94]
	)	
v.	)	
	)	
JANICE H. FAULKNER, et al.,	)	
	)	
Defendants.	)	

This matter is before the court on plaintiffs' motion for reconsideration. In an order filed May 6, 1994, this court granted defendants' motion for summary judgment and entered final judgment in favor of the defendants. Defendants have filed a memorandum in opposition to plaintiff's motion, and this matter is ripe for disposition.

Plaintiffs move for reconsideration on three grounds: that they need not satisfy state procedural law in order to maintain a suit in federal court for the deprivation of a federal

right pursuant to 42 U.S.C. § 1983; that this court has already held that the state statute did not satisfy due process; and that this court has the authority to require the creation of a nondiscriminatory taxing scheme.

The remedies for the collection of an unconstitutional tax are prospective injunctive relief, a pre- or post-deprivation remedy that satisfies the requirements of the due process clause, and meaningful backward-looking relief. McKesson v. Div. of Alcoholic Beverages & Tobacco, 100 S.Ct 2238 (1990). Accordingly, the state post-deprivation remedy, N.C. Gen. Stat. § 105-267, is not an administrative remedy or hurdle. It is, in fact, an integral part of the remedy to which plaintiffs are entitled. Federal law requires that when a tax is collected, there be a pre- or post-deprivation remedy for the tax that satisfies the due process clause. In other words, the state law which plaintiffs claim is an administrative requirement is, in fact, part of the remedy afforded to them by the federal constitution.

The North Carolina Supreme Court has already decided that N.C. Gen. Stat. § 105-267 gives plaintiffs due process, both on its face and as applied. This court is bound by that determination. Kremer v. Chemical Constr. Corp., 456 U.S. 461 (1986). Plaintiffs, however, contend that this court's finding that § 105-267 is not plain, speedy and efficient was a finding that the statute violates the due process clause. The court declines to adopt plaintiffs' reasoning. The due process clause and the Tax Injunction Act are different devices with different standards. Even if they were not, and this court had unwittingly held that § 105-267 violated the due process clause, this court's decision was non-final. Plaintiffs recognized this fact when they moved for the entry of final judgment. The state court judgment was, however, final, and therefore binding on this court.

Finally, plaintiffs argue that the court has full authority to create in hindsight a nondiscriminatory taxing scheme. The meaningful backward-looking relief discussed in McKesson was a monetary refund. The Eleventh Amendment bars suits for money damages, including refunds, against a state in a federal district court. Edelman v. Jordan, 415 U.S. 651 (1974). Consequently, plaintiffs request declaratory and injunctive relief in their motion for reconsideration. However, the allegedly unconstitutional taxing scheme has been repealed. There is no longer any practice to enjoin in this matter. Plaintiffs have received all the remedy a federal court exercising original jurisdiction is able to give to them.

For the foregoing reasons, plaintiffs' motion for reconsideration is DENIED.

This the 27th day of June, 1994.

/s/ Malcolm J. Howard
MALCOLM J. HOWARD
United States District Judge
I certify the foregoing to be a true and correct copy of the original. David W. Daniel, Clerk, United States District Court Eastern District of North Carolina

/s/ Cherlyn Wells
CHERLYN WELLS
Deputy Clerk

At Greenville, NC
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APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
RALEIGH DIVISION

NO. 89-282-CIV-5-H

NORMAN W. SWANSON, et al.,	)	
	)	
Class A Plaintiffs,	)	
	)	
CHARLES L. BERRY, et al.,	)	
	)	**ORDER**
Class B Plaintiffs,	)	[Filed: May 6, 1994]
	)	
v.	)	
	)	
JANICE H. FAULKNER, et al.,	)	
	)	
Defendants.	)	

This matter is before the court on numerous motions. The parties have fully briefed these matters, and the court heard extensive oral argument on February 15, 1994. This case is ripe for ruling.

STATEMENT OF THE CASE

Retired federal employees ("Class A Plaintiffs") and active duty military personnel and reservists ("Class B Plaintiffs") filed this action on April 14, 1989, to challenge

allegedly discriminatory North Carolina taxes. In February 1990, plaintiffs filed an action for money damages in the Wake County Superior Court. In an order filed August 16, 1990, this court held that the federal cause of action was not barred by the Tax Injunction Act, 28 U.S.C. § 1341, because the state remedy is not plain, speedy, and efficient; that comity did not prevent the court from exercising jurisdiction; and that the plaintiffs' claims for monetary relief were barred by the Eleventh Amendment. After an appeal to the United States Court of Appeals for the Fourth Circuit, which has no bearing on the motions currently before the court, plaintiffs' federal cause of action rested in a dormant state for nearly three years while the state court proceedings moved ahead.

The plaintiff's state court action was eventually decided in favor of defendants by the Supreme Court of North Carolina. Swanson v. North Carolina, 329 N.C. 576, 407 S.E.2d 791 (1991). Plaintiffs sought rehearing in the state court, arguing that Davis v. Michigan Dep't of Treasury, 489 U.S. 803 (1989), required judgment in their favor. In Davis, the United States Supreme Court ("Supreme Court") held that a tax similar to that complained of by plaintiffs violated principles of intergovernmental tax immunity. On rehearing, the state court adhered to its earlier decision on the grounds that Davis did not apply retroactively. Swanson v. North Carolina, 330 N.C. 390, 410 S.E.2d 490 (1991).

The Supreme Court granted certiorari, vacated the judgment of the North Carolina court, and remanded for further consideration in light of Harper v. Virginia Dep't of Taxation, 113 S. Ct. 2510 1993. Swanson v. North Carolina, 113 S. Ct. 3025 (1993). In Harper, decided in June of 1993, the Court held that the constitutional rule of Davis is to be applied retroactively. Id. at 2518. The Court also stated that the

appropriate relief was a pre-deprivation or post-deprivation remedy permitting the taxpayer to challenge the collection of the tax. Id. at 2519.

While awaiting the decision of the North Carolina Supreme Court, plaintiffs moved this court for the entry of final judgment on August 6, 1993. On September 7, 1993, defendants moved to dismiss, or in the alternative for reconsideration of this court's August 16, 1990 order. On December 30, 1993, defendants moved to dismiss on the grounds that plaintiffs' cause of action was moot. Plaintiffs moved for partial summary judgment on February 4, 1994.

The state court filed its third opinion in Swanson v. North Carolina, 335 N.C. 674, ___ S.E.2d ___, on March 4, 1994. The state supreme court held that the plaintiffs had failed to comply with the requirements of N.C. Gen. Stat. § 105-267; that statute, North Carolina's post-deprivation remedy provision, comported with due process as required by Harper; and that this court's August 16, 1990, order was not final and, therefore, would not collaterally estop the Supreme Court of North Carolina. The state court then remanded the case for entry of summary judgment for defendants. On March 7, 1993, defendants filed a motion for summary judgment in this court on the grounds of collateral estoppel or res judicata. On March 16, 1994, plaintiffs moved to sever their "Sheehy" claims or, in the alternative, for voluntary dismissal of those claims.

DISCUSSION

Summary judgment is authorized by Rule 56 of the Federal Rules of Civil Procedure. Summary judgment is appropriate where there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law.

Defendants move for summary judgment on the grounds that plaintiffs' claim is precluded by the decision of North Carolina Supreme Court in Swanson v. North Carolina, 335 N.C. 674, --- S.E.2d --- (1994).

Before addressing defendants' claim preclusion argument, however, it is important for the court to deal briefly with defendant's challenges to jurisdiction. It is axiomatic that a court cannot enter judgment without jurisdiction. However, this court has jurisdiction over the matter and the case is not moot, as prospective injunctive relief is available.[1] Accordingly, defendants' motion to dismiss or for reconsideration must be denied.

I. Claim and Issue Preclusion

Defendants assert that plaintiffs have already litigated the matters before this court in the state courts and lost, and that federal law requires this court to give the state judgment preclusive effect. The full faith and credit statute, 28 U.S.C. §

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[1] A federal court may only decide cases in which relief is available to plaintiffs. See, e.g., Taylor v. Rogers, 781 F.2d 1047 (4th Cir. 1986). The Eleventh Amendment permits a federal court to grant prospective relief against a state. Ex Parte Young, 209 U.S. 123 (1908). This court has the constitutional authority to strike down North Carolina's allegedly unconstitutional post-deprivation remedy, N.C. Gen. Stat. § 105-267, as violative of the due process clause.

The court is aware that a federal district court cannot declare a state tax statute unconstitutional in light of the Tax Injunction Act, 4 U.S.C. § 111. California v. Grace Brethren Church, 457 U.S. 393, 408 (1982). Striking down North Carolina's post-depreciation remedy, however, would not have the effect of suspending tax collection. It would alter the method by which taxpayers could protest illegal or unconstitutional taxation by the state, and so is permitted under the Tax Injunction Act.

1738, provides that state judicial proceedings are entitled to the same full faith and credit in all courts within the United States which they would have in the courts from which they were taken. Defendants are correct that § 1738 embodies principles of collateral estoppel and res judicata. "Section 1738 requires federal courts to give the same preclusive effect to state court judgments that those judgments would be given in the courts of the State from which the judgments emerged." Kremer v. Chemical Constr. Corp, 456 U.S. 461, 466 (1982). A federal district court is "to apply the law of the rendering state to determine whether and to what extent the state court judgment should have preclusive effect in the federal action." Davenport v. North Carolina Dep't of Transp., 3 F.3d 89, 92 (4th Cir. 1993).

Res judicata, or claim preclusion, bars relitigation of the same cause of action previously litigated in another forum. Bockweg v. Anderson, 333 N.C. 486, 428 S.E.2d 157 (1993). The related doctrine of collateral estoppel, or issue preclusion, prohibits the relitigation of matters actually litigated and determined in a different cause of action. Id. The doctrines are collectively referred to by many courts, including those of North Carolina, as res judicata. McInnis v. Hall, 318 N.C. 421, 427 n.1, 349 S.E.2d 552, 556 n.1 (1986). Claim and issue preclusion are the preferred terms in both federal and North Carolina courts. Id.

Defendants rely on both doctrines in support of their motion for summary judgment. Defendants' argument is brief, consisting of only one paragraph, and does not argue their point. The court must assume that defendants' motion alleges that the cause of action decided in the state court is identical to that in this federal court; defendants dispute this fact. In order to prevail on a claim of res judicata, or claim preclusion, under

North Carolina law, a party must show that the first suit proceeded to a final judgment on the merits; that the same cause of action is involved; and that the parties in the second suit are parties to, or in privity with, the parties in the first suit. McInnis, 318 N.C. at 429, 349 S.E.2d at 557.

Defendants dispute that the state and federal claims are identical. Even if defendants are correct, however, the related doctrine of issue preclusion, or collateral estoppel, mandates that this court grant summary judgment to defendants.

> Collateral estoppel applies when the following requirements are met: (1) The issues to be concluded must be the same as those involved in the prior action; (2) in the prior action, the issues must have been raised and actually litigated; (3) the issues must have been material and relevant to the disposition of the prior action; and (4) the determination made of those issues in the prior action must have been necessary and essential to the resulting judgment.

Beckwith v. Llewellyn, 326 N.C. 569, 574, 391 S.E.2d 189, 191 (1990).

Plaintiffs sued in state court to protest the collection of a tax as unconstitutional. Plaintiffs sued in federal court to protest the same tax. In both cases, the controlling issue was whether N.C. Gen. Stat. § 105-267 was a constitutional post-deprivation remedy as required by Davis v. Michigan, either on its face or as applied. Inasmuch as the same issues are involved, the first element of North Carolina's issue preclusion test is satisfied.

In the state action, the constitutionality of the state's post-deprivation remedy was raised and litigated extensively; it was the dispositive issue in the case. Therefore, the second element of the issue preclusion test is satisfied. The case could not have been decided without consideration of the issue, and so the third element of the test, whether the issue was material and relevant, is also satisfied. The fourth element is whether the issues decided were necessary and essential to the ultimate outcome of the case. The state case could not be resolved without a decision on the constitutionality of the post-deprivation remedy, and so the fourth element of the test is satisfied as well. The doctrine of collateral estoppel, also known as issue preclusion, requires that defendants' motion for summary judgment be granted.

Plaintiffs argue, however, that the state court decision cannot "reverse this Court's earlier Order." Pls.' Resp. to Defs.' Mot. to Dismiss at 5. Plaintiffs' argument rests on their assertion that the court's August 16, 1990, order was a ruling on the merits in plaintiffs' favor. The court finds that plaintiffs' argument must be rejected. Plaintiffs rely on Age Int'l v. Miller, 830 F. Supp. 1484 (N.D. Ga. 1993), for the conclusion that a finding that a post-deprivation remedy is not "plain, speedy and efficient" under the Tax Injunction Act is the equivalent of a finding that the remedy violates due process. In that case, the district court clearly stated that the Tax Injunction Act does not require all of "the same remedial bells and whistles that are required by the Due Process Clause." Id.

The Supreme Court recognizes that the Tax Injunction Act and the due process clause are different. A post-deprivation remedy is sufficient if it provides a taxpayer with a hearing and a judicial determination at which a taxpayer may raise constitutional objections to the tax. Rosewell v. LaSalle Nat'l

Bank, 450 U.S. 503 (1981). The Supreme Court did not expressly require that a tax violate due process before a district court lifted the Tax Injunction Act's procedural bar. Had the Court intended to do so, it would have. Instead, the Court required a full judicial hearing at which constitutional objections, including allegations of due process violations, could be raised and decided. Accordingly, the Tax Injunction Act is a jurisdictional statute, and it is not coterminous with the due process clause. This court's August 16, 1990 order cannot suppress the preclusive effect of the judgment of the Supreme Court of North Carolina.

This court's August 16, 1990, order was a finding for the purposes of jurisdiction under the Tax Injunction Act. It was not a determination that N.C. Gen. Stat. § 105-267 violated the due process clause. Plaintiffs litigated their due process claim in front of the state supreme court and lost. This court is required, as a matter of federal law, to give preclusive effect to a judgment of the North Carolina Supreme Court. To borrow the words of plaintiff, this court does feel somewhat like a "potted plant" in its inability to reach the merits of this case. However, the contours of American federalism and the Tax Injunction Act compel the result the court reaches today.

II. The "Sheehy" Claims

Plaintiffs also move the court to sever, or to grant voluntary dismissal, on their "Sheehy" claims. Plaintiffs allege that when North Carolina raised its retirement benefits, so as to give to state employees the same income they enjoyed under the discriminatory tax scheme struck down in Davis, it continued to discriminate against plaintiffs. In Sheehy v. Pub. Employees Retirement Div., 864 P.2d 762 (Mont. 1993), the state supreme court of Montana found that an increase in funding to state

pension benefits was, because it was part of a tax adjustment bill, a tax refund. The Montana court held that the tax refund violated the principles established in Davis by taxing in a discriminatory fashion on the basis of the source of the income.

A motion to sever is a matter committed to the discretion of the court. Arnold v. Eastern Airlines, 681 F.2d 186 (4th Cir. 1982). The court must weigh any genuine risk of prejudice or confusion against the necessity of trying the claims together. Molever v. Levenson, 539 F.2d 996 (4th Cir. 1976). Voluntary dismissal, or a plaintiff's motion for dismissal without prejudice, is also a matter of discretion. Davis v. USX Corp., 819 F.2d 1270 (4th Cir. 1987). "A plaintiff's motion . . . for dismissal without prejudice should not be denied absent substantial prejudice to the defendant." Andes v. Versant Corp., 788 F.2d 1033, 1036 (4th Cir. 1986).

In support of their motion, plaintiffs contend that, first, they require a brief period of additional discovery, and second, that plaintiffs expect defendants to immediately appeal this court's decision. Defendants assert that judicial economy requires that the claims be tried together. Defendants also emphasize the fact that discovery has been closed for some time. Defendants finally note that because plaintiffs presented their claim to the state supreme court, the same preclusion principles that govern the body of the case also control this issue.

Plaintiffs first presented the "Sheehy" claims to this court in 1993, nearly four years after filing suit. Defendants object to severance or dismissal on the grounds that they will be prejudiced by the reopening of discovery or being forced to defend themselves in a separate action by plaintiffs. Defendants have not expended significant effort, however, in defending the Sheehy claims. Those arguments were not presented to the

court until the state supreme court of Montana issued its ruling in 1993. In contrast, the prejudice to plaintiffs in prosecuting claims without adequate discovery might work a substantial hardship to them.

The court also notes that whatever the merits of plaintiffs' "Sheehy" claims might be, they are subject to the requirements of the North Carolina post-deprivation remedy, N.C. Gen. Stat. § 105-267. The constitutionality and applicability of that statute has already been decided by the North Carolina Supreme Court, and the issue preclusion bar applies to plaintiffs' "Sheehy" claims. It is not clear from the pleadings and memoranda, however, whether plaintiffs complied with the requirements of the post-deprivation remedy. Accordingly, either severance or dismissal without prejudice of the "Sheehy" claims is appropriate.

Neither voluntary dismissal nor severance would work substantial hardship on defendants. Defendants did not have to defend the "Sheehy" claims until plaintiffs raised them in 1993. Dismissal without prejudice will permit plaintiffs to assess their case and properly plead it, should they elect to refile. Because motions for voluntary dismissal are to be freely granted, the court will grant plaintiffs' motion for voluntary dismissal.

CONCLUSION

For the foregoing reasons, defendants' motion to dismiss or for reconsideration is DENIED. Plaintiffs' motion to sever is DENIED. Plaintiffs' motion to dismiss without prejudice their claim for relief based on Sheehy v. Pub. Employees Retirement Div., for the taxable years 1990 to the present, is GRANTED. Defendants' motion for summary judgment is GRANTED as to all other claims remaining before the court. Plaintiffs' motions

for partial summary judgment and for the entry of final judgment are, accordingly, DENIED. Inasmuch as all matters before the court are concluded, the court ORDERS entry of final judgment in favor of defendants. The clerk is directed to close this case.

This the 4th day of May, 1994.

/s/ Malcolm J. Howard
MALCOLM J. HOWARD
United States District Judge

I certify the foregoing to be a true and correct copy of the original. David W. Daniel, Clerk, United States District Court Eastern District of North Carolina

/s/ Cherlyn Wells
CHERLYN WELLS
Deputy Clerk

At Greenville, NC
#16

APPENDIX D

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NORTH CAROLINA
RALEIGH DIVISION

No. 89-282-CIV-5-H

NORMAN W. SWANSON, *et al.*,
Class A Plaintiffs,

Charles L. Berry, Robert D. Lennon, Zebulon V. Moseley, III, Gary W. O'neal, Milton S. Price, Martin L. Speicher, and Paul H. Turney,
Class B Plaintiffs,

v.

Helen A. Powers, Secretary of The North Carolina Department Of Revenue, The North Carolina Department Of Revenue, and Harlan Boyles, Treasurer Of The State Of North Carolina,

Defendants.

ORDER

[Filed August 16, 1990]

This matter is before the court on the defendants' motion to dismiss for lack of subject matter jurisdiction and failure to

state a claim pursuant to Fed. R. Civ. P. 12(b) (1) and 12(b) (6). For the reasons discussed below, the court grants the motion in part and denies it in part.

FACTS

The Class A Plaintiffs are retired federal employees who challenge former North Carolina income tax laws that treated the income of retired federal employees less favorably than the income of retired state employees. Federal retirement income was subject to a partial exemption, but state retirement income was exempted completely. This taxing scheme is indistinguishable from that struck down by the Supreme Court in *Davis v. Michigan Dep't of Treasury*, _____ U.S. ____, 109 S. Ct. 1500, 103 L.Ed.2d 891 (1989), under 4 U.S.C. § 111 and the principle of intergovernmental tax immunity. The plaintiffs allege that the state's administration of its income tax laws deprive them of their civil rights in violation of 42 U.S.C. § 1983, 4 U.S.C. § 111, and the equal protection and due process clauses of the United States Constitution.

Class B plaintiffs are active-duty military personnel and reservists who challenge the statutory $1500 annual income tax exclusion for compensation paid to members of the North Carolina National Guard. Both classes seek damages in the form of refunds, a declaration that the collection of tax on such income violates federal law, and an injunction barring the defendants from collecting such taxes in the future.

The defendants have filed this motion to dismiss for lack of subject matter jurisdiction and failure to state a claim. The parties have extensively briefed the issues, and the court has conducted a lengthy hearing. Accordingly, the motion is ripe for ruling.

DECISION

I. *The Tax Injunction Act*

The defendants contend that this action is barred by the Tax Injunction Act of 1937, 28 U.S.C. § 1341, which provides:

> The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.

This statute applies to requests for declaratory relief, injunctive relief, and damages. *See California v. Grace Brethren Church*, 457 U.S. 393, 102 S. Ct. 2498, 73 L.Ed.2d 93 (1982); *Moss v. Georgia*, 655 F.2d 668 (5th Cir. 1981). The plaintiffs invoke the federal instrumentalities exception to the Tax Injunction Act. Alternatively, the plaintiffs contend that the state remedy is not plain, speedy, and efficient.

Under the federal instrumentalities exception, the Tax Injunction Act does not bar actions in which the United States or one of its instrumentalities is the plaintiff. *See, e.g., Dep't of Employment v. United States*, 385 U.S. 355, 87 S. Ct. 464, 17 L.Ed.2d 414 (1966). The parties have cited to the court no federal cases holding that employees are or are not instrumentalities. The plaintiffs rely on language in *Davis* tracing the development of the right of federal employees to invoke the doctrine of intergovernmental tax immunity. The plaintiffs argue that under *Davis* the definition of a federal instrumentality is co-extensive with taxpayers protected by intergovernmental tax immunity and 4 U.S.C. § 111.

The court finds, however, that federal employees are not federal instrumentalities exempted from the Tax Injunction Act. *Davis*, which began in the Michigan state courts, does not address the applicability of the Tax Injunction Act. The Court did, as the plaintiffs suggest, outline the development of the taxation of the employees of one sovereign by another. In so doing, the Court stated that 4 U.S.C. § 111 codified *Graves v. New York*, 306 U.S. 466, 59 S. Ct. 595, 83 L.Ed. 927 (1939). It is clear from *Graves* that federal employees were exempt from state taxation not because they were federal instrumentalities, but because they were employees of instrumentalities. 306 U.S. at 483 n.2, 485. *See also New York v. Graves*, 299 U.S. 401, 408, 57 S. Ct. 269, 272, 81 L.Ed. 306 (1937).[1]

Because intergovernmental tax immunity cases draw a definitional distinction between instrumentalities and their employees, the court concludes that a similar distinction exists under the Tax Injunction Act. This conclusion is supported by the fact that all cases applying the instrumentalities exception involve entities that are clearly distinguishable from the individual plaintiffs in this action. *See, e.g., Dep't of Employment*, 385 U.S. at 359; *Federal Reserve Bank v. Comm'r of Corporations and Taxation*, 499 F.2d 60 (1st Cir. 1974);

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[1] In *United States v. New Mexico*, 455 U.S. 720, 102 S. Ct. 1373, 71 L.Ed.2d 550 (1982), the Court held that independent contractors are not federal instrumentalities protected by the doctrine of intergovernmental tax immunity. The Court drew a distinction between independent contractors and employees, whom the court described as "constituent parts" of the United States. *New Mexico*, 455 U.S. at 740, 102 S. Ct. at 1386. A possible interpretation of this case is that employees are instrumentalities. However, this case did not involve the Tax Injunction Act; rather, it seems to be consistent with the prior line of cases holding that federal employees are protected by intergovernmental tax immunity because they are employees of instrumentalities, not because they are themselves instrumentalities.

Federal Land Bank v. Bd. of County Comm'rs, 582 F.Supp. 1507 (D.Colo. 1984); *First Nat'l Bank v. Dickinson*, 291 F.Supp. 855 (N.D.Fla. 1968), *affirmed*, 393 U.S. 409, 89 S. Ct. 685, 21 L.Ed.2d 634 (1969). Moreover, several identical actions brought in federal court by federal employees have been dismissed pursuant to the Tax Injunction Act. *Waldron v. Collins*, 788 F.2d 736 (11th Cir.), *cert. denied*, 479 U.S. 884, 107 S. Ct. 274,93 L.Ed.2d 250 (1986); *Todd v. Johnson*, 718 F.Supp. 1305 (S.D. Miss. 1989); *Melof v. Hunt*, 718 F.2d 877 (M.D.Ala. 1989).[2] Accordingly, the court finds that the plaintiffs are not federal instrumentalities exempted from the Tax Injunction Act.

The court finds, however, that the state remedy is not plain, speedy, and efficient. A plain, speedy, and efficient remedy is one that provides a taxpayer with a full hearing and judicial determination at which he or she may raise any and all constitutional objections. *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 513, 101 S. Ct. 1221, 67 L.Ed.2d 464 (1981). The state remedy does not have to be equal to the federal remedy. *Ayers v. Polk County*, 697 F.2d 1375, 1377 (11th Cir. 1983). A state remedy is inadequate, however, if some "uncertainty" surrounds it. *Rosewell*, 450 U.S. at 516-17. The plaintiffs contend that the defendants have so confused the state remedy that it is impossible to enforce the plaintiffs' federal rights in state court.

The uncertainty surrounds the statute of limitations. The defendants contend that the plaintiffs' state remedy is governed by N.C. Gen. Stat. § 105-267, which provides that a taxpayer contesting the illegality of a tax must pay the tax and then file a

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[2] None of these cases specifically addressed the federal instrumentalities exception.

written demand for refund within 30 days. If the refund is denied, the taxpayer has three years to file an action in the Superior Court of Wake County or the county of the taxpayer's residence. On its face, this remedy is plain, speedy, and efficient. *See Grace Brethren Church*, 457 U.S. at 412.

Confusion arises, however, out of the existence of N.C. Gen. Stat. § 266.1, which provides that taxpayers may file for refunds for mathematical or other errors within three years of payment. If no refund is given, the taxpayer has 90 days to file an action in the Superior Court of Wake County or the county of residence. The two statutes address different situations. Section 267 provides a remedy by which to contest illegal or unconstitutional taxes; section 266.1 provides a remedy by which to receive refunds for overpayment caused by mathematical or other errors. *Coca-Cola Co. v. Coble*, 293 N.C. 565, 238 S.E.2d 780 (1977).

This remedy is uncertain because of the conduct of the individual defendants and the Department of Revenue. All interpretation and explanation of these statutes provided to taxpayers by the defendants indicated that *any* request for refund may be made within three years of payment. This information was provided in "Individual Tax Income Bulletins" published by the Department of Revenue. Plaintiffs' Memorandum, Exhibit 2. The defendants' instruction booklets are to the same effect. Moreover, after *Davis* was decided, the Department of Revenue announced publicly that refunds of taxes paid within three years would be allowed under the customary practice. Plaintiffs' Memorandum, Exhibits 33,34. Taxpayers were not told of the 30-day rule until four days before the filing deadline for 1989, well after many of the plaintiffs had filed their returns.

The defendants, soon after the filing of 1989 tax returns, began denying *Davis* refund requests pursuant to the 30-day statute of limitations of section 267. They also raise this statute as a defense in related state court litigation and in this action. The defendants have thereby deprived the plaintiffs a full hearing and judicial determination of their claims. *Rosewell*, 450 U.S. at 513.

A further complication is that the defendants cannot administer the 30-day rule. The defendants do not date-stamp returns filed prior to the deadline. The defendants assume that the date the return is signed is the date of payment, regardless of when the return was filed. Therefore, those plaintiffs filing their returns more than 30 days after signing the returns never had the opportunity to file a claim.

The state remedy is also inadequate because it does not provide for a class action, thereby requiring individual litigation of thousands of refund claims. Each of the claims is small enough to make the cost of such litigation prohibitive. The plaintiffs estimate that Class A contains 89,111 members and that Class B contains 49,486 members. (Exhibits 10, 11, and 12). At the hearing, plaintiffs' counsel estimated the average refund to be approximately $700. Some courts have held that the unavailability of class actions does not in itself render the state remedy inadequate. *See, e.g., Waldron*, 788 F.2d at 738. The court finds, however, that the absence of a class action procedure may be considered along with all other facts in determining whether the state remedy is adequate for purposes of the Tax Injunction Act.

The remedy provided by the state to the Class A Plaintiffs is the recently-enacted N.C. Gen. Stat. § 105-151.20. Pursuant to this statute, federal retirees who paid state income

tax on federal retirement income for the taxable year 1988 may claim a tax credit in that amount in equal installments over a three-year period beginning with the taxable year 1990. This remedy is inadequate because it fails to take into account the time value of the plaintiff's money. The state is in essence admitting that the tax was improper, but some of the money will not be returned until five years after payment.[3] Furthermore, given that these plaintiffs are retirees, it is reasonable to assume that a certain number of them will die in the next three years and will never receive their money. Others may have no tax liability from 1990-1992 and so will be unable to use the credit. In reality, this remedy provides the class with only a partial refund. *See Georgia Railroad & Banking Co. v. Redwine*, 342 U.S. 299, 303, 72 S. Ct. 321, 324, 96 L.Ed.2d 335 (1952) (remedy is inadequate if only partial refund will be recovered).[4] This statute provides no remedy to the Class B plaintiffs.

For the above-stated reasons, the court finds that the state remedy is not plain, speedy, and efficient. *Hillsborough v. Cromwell*, 326 U.S. 620, 624-26, 66 S. Ct. 445, 90 L.Ed. 358

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[3]The Court in *Rosewell* held that the state's failure to pay interest and the unavoidable delay in the litigation process did not prohibit the remedy from being speedy or efficient. 450 U.S. at 517-22, 101 S. Ct. at 1231-33. The defendants, however, are doing more than not paying interest; they are intentionally extending the period for refund through as late as April 15, 1993. This delay is not the unavoidable result of litigation, but is the intentional choice of the state legislature.

[4] Furthermore, this legislation, enacted after *Davis*, treats federal retirees differently than other taxpayers in that the retirees must receive their refunds over three years instead of in a lump sum payment. This legislation was enacted after the parties filed their briefs such that the parties have not addressed the issue of whether this remedy is an ongoing constitutional violation. *See* Footnote 5, *infra*.

(1946). Therefore, this action is not barred by the Tax Injunction Act.

II. Comity

Since the court has found that the state remedy is not plain, speedy, and efficient for purposes of the Tax Injunction Act, it necessarily follows that the remedy is not plain, adequate, and complete for purposes of comity. *See Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100, 116, 102 S. Ct. 177, 70 L.Ed.2d 271 (1981). Therefore, comity does not bar the court from exercising jurisdiction over this action.

III. Eleventh Amendment

The plaintiffs' claims for monetary damages in the form of refunds are barred by the eleventh amendment. *Edelman v. Jordon*, 415 U.S. 651, 94 S. Ct. 1347, 39 L.Ed.2d 662 (1974). The plaintiffs attempt to characterize their action as one for "equitable restitution." The Supreme Court has stated, however, that plaintiffs may not circumvent the eleventh amendment by characterizing a damages claim as one for equitable restitution. *Edelman*, 94 S. Ct. at 1356. It has long been established that unconstitutional taxes may not be recovered from the state treasury. *Great Northern Life Ins. Co. v. Read*, 322 U.S. 47, 64 S. Ct. 873, 88 L.Ed 1121 (1944); *Smith v. Reeves*, 178 U.S. 436, 20 S. Ct. 919, 44 L.Ed. 1140 (1900).

The plaintiffs contend that federal courts may order relief that has some effect on the state treasury. For example, in *Milliken v. Bradley*, 433 U.S. 267, 289, 97 S. Ct. 2749, 2761-62, 53 L.Ed.2d 745 (1977), a federal court ordered a state to spend $5.8 million to upgrade its educational system. In *Papasan v. Allain*, 478 U.S. 265, 282, 106 S. Ct. 2932, 2942,

92 L.Ed.2d 209 (1986), the Court distinguished between the expenditure of state funds necessary for future compliance with a court order and awards for accrued monetary liability. A federal court may order the former type of relief, but not the latter. It is clear, however, that the plaintiffs are seeking an award for monetary liability, which is precisely what the eleventh amendment forbids.

The plaintiffs suggest as a possible remedy a tax credit applied to future tax years. Substantively, however, this remedy is still one for accrued monetary liability that would be satisfied out of the general revenues of the state. The plaintiffs cannot avoid the eleventh amendment by receiving their award in the form of future tax credits, rather than present cash payments.

The plaintiffs contend finally that the eleventh amendment does not bar their damages claims because they are federal instrumentalities. *See, e.g., United States v. Mississippi*, 380 U.S. 128, 140-41, 85 S. Ct. 808, 814-15, 13 L.Ed.2d 717 (1965); *FDIC v. New York*, 732 F.Supp. 26 (S.D.N.Y. 1990). The court previously ruled, however, that federal employees are not federal instrumentalities. *Supra*, pp. 3-5. Therefore, the court must dismiss the damages claims against the defendants in their official capacities.[5]

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[5] The eleventh amendment does not bar the damages claims against Powers in her individual capacity. *Scheuer v. Rhodes*, 416 U.S. 232, 237-38, 94 S. Ct. 1683, 1687 (1974). Nor does it bar the claims for injunctive and declaratory relief necessary to correct an ongoing constitutional violation. *Green v. Mansour*, 474 U.S. 64, 68, 106 S. Ct. 423,426,88 L.Ed.2d 371 (1985).

IV. Powers' Qualified Immunity

The defendant Powers contends that she is protected from the damages claims by the doctrine of qualified immunity. Powers is shielded from liability if she can show that her conduct did not "violate clearly established statutory or constitutional rights of which a reasonable person would have known." *Harlow v. Fitzgerald*, 457 U.S. 800, 818, 102 S. Ct. 2727, 73 L.Ed.2d 396, 410 (1982). It must be objectively discernible in light of the law as it then existed that the defendant's conduct would violate that right. *Anderson v. Creighton*, 483 U.S. 635, 107 S. Ct. 3034, 97 L.Ed.2d 523 (1987).

Powers contends that the *Davis* decision established a new rule of law. The court finds, however, that the doctrinal underpinnings of *Davis* are long-standing principles. Intergovernmental tax immunity has its genesis in *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819). Similarly, 4 U.S.C. § 111, which plainly allows for only non-discriminatory taxation of federal employees, was enacted in 1939.

The substance of the defendant's argument is that she should not be required to forecast Supreme Court decisions at the risk of personal liability. In the court's opinion, however, *Davis* was inevitable. State officials should not be allowed to continue blatantly unconstitutional conduct until the courts specifically rule it unconstitutional. Powers had the statutory responsibility to regulate, monitor, advise, and act upon problems in administering the state tax code. *See* N.C. Gen. Stat. §§ 143B-218, 143B-219, 147-88, 105-257, and 105-453. Nevertheless, she collected unconstitutional taxes that she should have known were unconstitutional.

Soon after the enactment of 4 U.S.C. § 111, the North Carolina Attorney General reported in a February 12, 1940, Memorandum to the Commissioner of Revenue that section 111 "gives the consent of Congress to *non-discriminatory state taxation* of the compensation of Federal employees." Plaintiffs' Memorandum, Exhibit 14. The state instituted its discriminatory tax scheme in 1941; potential problems were first noted in a 1941 *North Carolina Law Review* article: "This may be permissible with respect to such state taxes as the income tax (unless it eventually face [s] trouble because of non-exemption for other annuities)." 19 N.C.L.Rev. 435, 519 (1941). Furthermore, on or about July 29, 1988, the defendant's office received a report from the Federation of Tax Administrators which included a two-page discussion of *Davis v. Michigan*. Finally, the discrepancy between federal and state retirement pay taxation was the subject of internal discussions throughout 1988 and 1989. Plaintiffs' Memorandum, Exhibits 18 (Letter from Department of Revenue to Legislative Counsel for the Governor) and 19 (Tax Fairness Commission Report of January 11, 1989).

Powers now asserts that it was unclear until *Davis* whether retired [sic] benefits were compensation for purposes of the Public Salary Tax Act. The *Davis* Court, however, found it obvious that retirement benefits were compensation. 109 S. Ct. at 1504. Moreover, it has been long-settled in North Carolina that retirement benefits are compensation. *See e.g. Bridges v. Charlotte*, 221 N.C. 472, 20 S.E.2d 825 (1942). Indeed, the defendant received withholdings on federal retirement benefits pursuant to a state statute authorizing income taxes from "wages" of federal employees. N.C. Gen. Stat. § 105-163.23. The court finds, therefore, that the defendant failed to recognize the legality of her conduct and that

her conduct violated clearly established federal rights of which a reasonable person should have been aware.

CONCLUSION

Accordingly, for the reasons discussed above, it is hereby ORDERED that the defendants' motion to dismiss pursuant to the Tax Injunction Act and principles of comity is DENIED. The motion to dismiss pursuant to the eleventh amendment is GRANTED as to the claims for monetary relief against the state and DENIED as to all other claims. The motion of the defendant Powers to dismiss pursuant to the doctrine of qualified immunity is DENIED.

This the 15th day of August, 1990.

/s/ Malcolm J. Howard
MALCOLM J. HOWARD
United States District Judge

At Greenville, NC
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APPENDIX E

IN THE SUPREME COURT OF NORTH CAROLINA

NORMAN W. SWANSON, et al., Class A Plaintiffs, CHARLES L. BERRY, et al., Class B Plaintiffs, vs. THE STATE OF NORTH CAROLINA, HELEN A. POWERS, Individually, BETSY Y. JUSTUS as Secretary of THE NORTH CAROLINA DEPARTMENT OF REVENUE, THE NORTH CAROLINA DEPARTMENT OF REVENUE and HARLAN BOYLES, TREASURER OF THE STATE OF NORTH CAROLINA, Defendants.	**[Filed 3/4/94]** **In the Office of Clerk Supreme Court of North Carolina** **No. 64PA91-Wake**

On remand from the United States Supreme Court. Heard in the Supreme Court 17 November 1993.

Womble Carlyle Sandridge & Rice, by G. Eugene Boyce, and Charles H. Taylor for plaintiff-appellees.

Michael F. Easley, Attorney General, by Edwin M. Speas, Jr., Senior Deputy Attorney General, Thomas F. Moffitt and Norma S. Harrell, Special Deputy Attorneys General, and Marilyn R. Mudge, Assistant Attorney General, for defendant-appellants.

EXUM, Chief Justice.

This is an action by plaintiffs, former federal employees and active duty federal military personnel and reservists, for the refund of certain income taxes paid by them before the 28 March 1989 decision of the United States Supreme Court in *Davis v Michigan Department of Treasury*, 489 U.S. 803, 103 L. Ed. 2d 891 (1989) We conclude the action may not be maintained because plaintiffs failed to comply with the procedural prerequisites of N.C.G.S. § 105-267 (1992). We, therefore, reverse the entry of summary judgment for plaintiffs entered by the trial court and remand for entry of judgment for defendants dismissing the action.

Before *Davis*, twenty-three states, including North Carolina, exempted retired state employees from payment of income tax on pension benefits. Retired federal employees were exempt from payment of state income taxes on the first $3,000 of their pension benefits. There was no exemption for beneficiaries of private pensions. As of 1979, the first $1,500 of income for members of the North Carolina National Guard was excluded from taxation. In 1989, the State amended this benefit

so that members of the National Guard received a $1,500 deduction. The State conferred no comparable benefit on members of the federal armed forces.

In *Davis* the United States Supreme Court held that a state statute exempting state employees' retirement benefits from taxation but not granting the same exemption to their federal counterparts violated the constitutional doctrine of intergovernmental tax immunity and 4 U.S.C. §111 (1989). Under section 111 the federal government "consents to [state] taxation of pay or compensation for personal service as an officer or employee of the United States . . . if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation." 4 U.S.C. § 111.

Responding to Davis, the North Carolina General Assembly amended its taxation scheme. First, it repealed the tax exemption for the retirement benefits of state employees retroactive to 1 January 1989 and created a $4,000 exclusion for the retirement benefits of both state and federal employees. N.C.G.S. § 105-134.6(b) (1992). Second, it authorized federal retirees to claim a tax credit on their 1990, 1991, and 1992 income taxes for taxes paid in 1988 on their federal pensions. N.C.G.S. § 105-151.20 (1992). Third, it repealed the $1,500 deduction for National Guard compensation. 1989 N.C. Sess. Laws, ch. 1002 (1990).

This is the third time this case has come before us. We first held plaintiffs were not entitled to the refunds claimed because the decision in *Davis* did not apply retroactively. *Swanson*, 329 N.C. 576, 407 S.E.2d 791 (1991) (*Swanson I*). Next we concluded, on rehearing, that certain provisions in our state constitution afforded plaintiffs no relief, and we reaffirmed our earlier decision. *Swanson*, 330 N.C. 390, 410 S.E.2d 490

(1991) (*Swanson II*). The result of the *Swanson* decisions was to reverse the trial court's order granting Plaintiffs income tax refunds for the years 1986 through 1989 and to dismiss plaintiffs' action.

Plaintiffs then petitioned the United States Supreme Court for review of the *Swanson* decisions. On 28 June 1993, the United States Supreme Court granted plaintiffs' petition for writ of certiorari, vacated our decisions in *Swanson I* and *Swanson II*, and remanded the case for further consideration in light of its holding in *Harper v. Virginia Department of Taxation*, 509 U.S. ___, 125 L. Ed. 2d 74 (1993), that *Davis* must be applied retroactively. *Swanson v. North Carolina*, ___ U.S. ___ 125 L. Ed. 2d 713 (1993).

Plaintiffs moved this Court to remand the case to superior court "for implementation of orders previously entered," or, alternatively, for additional briefing and argument on the meaning and effect of *Harper*. On 29 July 1993, the Court denied plaintiffs' motion for remand, granted plaintiffs' alternative motion and directed the parties to file additional briefs on the remaining issues pending before this Court and any other issues raised by *Harper*.

I.

Plaintiffs contend they are entitled to full refunds for income taxes paid by them on pension benefits for the tax years 1985 through 1988 pursuant to North Carolina's taxation statutes held unconstitutional in *Davis*. We conclude plaintiffs are procedurally barred from recovering in this action the refunds sought because they did not comply with the State's statutory postpayment refund demand procedure.

The sole procedure by which a North Carolina taxpayer may challenge the legality of any tax is as follows:

> No court of this State shall entertain a suit of any kind brought for the purpose of preventing the collection of any tax imposed in this Subchapter. Whenever a person shall have a valid defense to the enforcement of the collection of a tax assessed or charged against him or his property, such person shall pay such tax to the proper officer, and such payment shall be without prejudice to any defense of rights he may have in the premises. *At any time within 30 days after payment, the taxpayer may demand a refund of the tax paid in writing from the Secretary of Revenue* and if the same shall not be refunded within 90 days thereafter, may sue the Secretary of Revenue in the courts of the State for the amount so demanded. Such suit may be brought in the Superior Court of Wake County, or in the county in which the taxpayer resides at any time within the three years after the expiration of the 90-day period allowed for making the refund. If upon the trial it shall be determined that such a tax or any part thereof was levied or assessed for an illegal or unauthorized purpose, or was for any reason invalid or excessive, judgment shall be rendered therefor, with interest, and the same shall be collected as in other cases. The amount of taxes for which judgment shall be rendered in such action shall be refunded by the State; provided, nothing in this section shall be construed to conflict with or supersede the provisions of G.S. 105-241.2.

N.C.G.S. § 105-267 (emphasis added).

In *Bailey v. North Carolina*, 330 N.C. 227, 412 S.E.2d 295 (1991), *cert. denied*, ___ U.S. ___, 118 L. Ed. 2d 547 (1992), this Court held that "[w]hen a tax is challenged as unlawful rather than excessive or incorrect, the appropriate remedy is to bring suit under N.C.G.S. § 105-267." *Id.* at 235, 412 S.E.2d at 300. That the challenge is to the constitutionality of the tax does not exempt a taxpayer from following the statute's mandatory procedure. *Id.* Failure to comply with the requirements in section 105-267 bars a taxpayer's action against the State for a refund of taxes. *Id.* at 236, 412 S.E.2d at 301.

The plaintiffs in Bailey, state and local government employees whose retirement benefits had vested, brought suit against the State, claiming it had violated assurances that their benefits would be exempt from state income tax. We held that "[i]nsofar as plaintiffs' complaint seeks a refund of 1989 taxes paid, it should have been dismissed for failure of plaintiffs to satisfy conditions precedent to such an action as required by N.C.G.S. § 105-267." *Id.* at 234, 412 S.E.2d at 300. We said:

> A taxpayer with "a valid defense to the enforcement of the collection of a tax" must first pay the tax, then demand a refund of that tax in writing within thirty days after payment. Only when the Secretary of Revenue fails to refund the tax within ninety days may the taxpayer sue the Secretary of Revenue for the amount demanded. Absent protest in the form of a demand for refund, a tax is voluntarily paid, and "voluntary payments of unconstitutional taxes are not refundable." *Coca-Cola Co. v. Coble*, 293 N.C. [565,] 569, 238 S.E.2d [780,] 783.

> The right to sue in a conditional right; the terms prescribed are conditions precedent to the institution of the action. Plaintiffs must allege and prove they demanded a refund within thirty days after payment. Failure to do so forfeits the right to sue. *Kirkpatrick v. Currin, Comr. of Revenue*, 250 N.C. [213,] 216, 108 S.E.2d [209,] 211; *Stenhouse v. Lynch*, 37 N.C. App. 280, 281, 245 S.E.2d 830, 831 (1978).

Id. at 236, 412 S.E.2d at 301. The purpose for this statutory protest requirement is that,

> Where protest has been interposed, the [taxing authority] is notified that it may be obliged to refund the taxes and is required to be prepared to meet that contingency. If no protest has been lodged, it is generally assumed that taxes paid can be retained to meet authorized public expenditures, and financial provision is not made for contingent refunds.

Id. at 238, 412 S.E.2d at 302 (quoting *Conklin v. Town of Southampton*, 141 A.D.2d 596, 598, 529 N.Y.S.2d 517, 519 (1988) (quoting *Mercury Mach. Importing Corp. v. City of New York*, 3 N.Y.2d 418, 426, 144 N.E.2d 400, 404, 165 N.Y.S.2d 517, 521 (1957)).

In *Bailey* all demand letters sent to the Secretary of Revenue were preceded by the plaintiffs' complaint. *Id.* at 237, 412 S.E.2d at 301. The Court held the plaintiffs' "demands for refunds followed neither the letter of the statute nor the reasonable criteria required by the Secretary of Revenue and were properly rejected and deemed invalid for purposes of suing

for refunds under N.C.G.S. § 105-267." *Id.* at 238-39, 412 S.E.2d at 302.

Here plaintiffs sent a "class demand letter" on 14 April 1989 to Helen A. Powers, Secretary of the North Carolina Department of Revenue, requesting refund of all income taxes paid on pension benefits for tax years 1985 to 1989. A second class demand letter was sent to Secretary Powers on 18 April 1989. On 11 July 1989 Secretary Powers responded to plaintiffs' letters of demand as follows:

> In order to constitute a valid demand for refund under G.S. 105-267, a taxpayer's request must include sufficient information to permit the Department to determine whether a refund may be made and, if so, in what amount. Such information would normally consist of the taxpayer's name and social security number, the year for which the tax was paid, the date on which the return was filed or the tax was paid, and the amount of federal retirement income received by the taxpayer during the year.
>
> To the extent that your letters furnish information concerning the named taxpayers sufficient to determine the amount of tax which they paid with respect to the federal retirement income for each year in question, the Department will, pursuant to G.S. 105-267, issue refunds for any such tax paid by those persons within the thirty days preceding the date of your letter.

> To the extent that your letter makes demand for refund of taxes paid by unnamed persons or by named persons not sufficiently identified to permit a determination as to their liability, your letter will not be considered a valid demand for refund, and no refunds will be issued.[1]

Plaintiffs filed this suit against Secretary Powers in her official capacity and individually on 16 March 1990 seeking refund of income taxes paid on pension benefits from 1985 to 1989. Thereafter, on 12 April 1990 plaintiffs sent a similar third class demand letter to Secretary Powers. Secretary Powers responded to plaintiffs' third demand letter by stating,

> Your letter does not identify any individual taxpayer, nor does it furnish information sufficient to determine the amount of tax which any taxpayer paid with respect to federal military or retirement income for any of the taxable years in question. Accordingly, your letter will not be considered a valid demand for refund, and no refunds will be issued.

The three class demand letters filed by plaintiffs were invalid protests and, as such, did not satisfy the requirements of section 105-267. "N.C.G.S. § 105-267 does not expressly prohibit taxpayers from seeking refunds as a class"; however, "it includes no provision for a tax refund demand to be made either by taxpayers as a class or as represented by others." *Id.* at 237,

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[1] As of 19 February 1990 the State, presumably pursuant to this letter, had refunded $9,145,523.92 to 12,404 taxpayers in plaintiff classes who timely filed refund requests pursuant to section 105-267. The State denied approximately $8,000,000 of refunds for 1988 taxes paid by taxpayers in plaintiff classes.

412 S.E.2d at 301. "Even when taxpayers are seeking a tax refund as a class, the requisites of N.C.G.S. § 105-267 must be met." *Id.* (footnote omitted). Plaintiffs' action "cannot be maintained unless preceded by an individual notice, protest or demand." *Id.* at 239 n.4, 412 S.E.2d at 202 n.4. "[A]bsent specific statutory authorization for class or representative tax refund demands, such [class] demands are ineffectual to satisfy this condition precedent to legal action for a tax refund under N.C.G.S. § 105-267." *Id.* at 240, 412 S.E.2d at 303.[2]

The only demands for tax refunds alleged or proved in this action are the class demand letters which we described above. Since these class demand letters do not constitute refund demands as required by section 105-267, this necessary prerequisite to filing this action against the State for the refunds claimed has not been met. The action therefore must be dismissed provided these procedures comport with constitutional due process, a question we now address.

II.

Plaintiffs contend the statutory refund procedure transgresses the Due Process Clause of the Fourteenth Amendment of the United States Constitution insofar, as it bars full refunds to plaintiffs for tax years 1985 through 1988 which, plaintiffs contend, are required by the United States Supreme Court's decision in *Harper v. Virginia Department of Taxation*, 509 U.S. ___ 125 L. Ed. 26 74.

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[2] Plaintiffs contend section 105-267 unconstitutionally denies them the right to bring a class action suit. We disagree. Once taxpayers have individually met the requirements of section 105-267, they are free to pursue their claim as a class.

We do not agree. Rather, we conclude that in light of both *Harper* and *McKesson Corporation v. Division of Alcoholic Beverage and Tobacco*, 496 U.S. 18, 110 L. Ed. 2d 17 (1990), the refund procedure provided in section 105-267 is free from any constitutional infirmity. It may, therefore, effectively bar actions for refunds in the tax years for, which the procedure was not followed.

Admittedly, this statute does not permit North Carolina taxpayers to challenge the legality, or constitutionality, of a tax before paying the tax. It does not, in other words, provide for a predeprivation remedy for the taxpayer. Instead it requires the taxpayer first to pay the tax sought to be challenged; second, to demand within 30 days of payment that the tax be refunded; and third, if the state refuses within 90 days to make the refund, the taxpayer must bring suit against the state for the refund within three years of the expiration of the 90-day period. As we have shown above, the timely demand for refund is a prerequisite for bringing suit against the State to recover the challenged tax.

We are convinced this procedure comports with due process under the United States Supreme Court's jurisprudence on the subject as it relates to taxation. That Court has long held that postdeprivation remedies in the area of taxation can comport with due process. *Cheatham v. United States*, 92 U.S. 85, 89-90, 23 L. Ed. 561, 562-63 (1875) (government has right to prescribe conditions on which it will subject itself to judgment of the courts in collection of revenues); *Dodge v. Osborn*, 240 U.S. 118, 122, 60 L. Ed. 557, 560 (1916) (requirement that taxes be paid and administrative procedures exhausted before suit for recovery could be filed does not violate due process); *Bob Jones University v. Simon*, 416 U.S. 725, 747, 40 L. Ed. 26 496, 515 (1974) (congressional restriction to postenforcement review of an organization claiming tax-exempt status is not

constitutionally infirm in light of the powerful government interests in protecting the administration of the tax system from premature judicial interference).

The principle that due process does not require predeprivation remedies in the area of taxation was most recently reaffirmed in *McKesson*, 496 U.S. 18, 110 L. Ed. 2d 17. The *McKesson* Court held postdeprivation remedies for tax refunds are sufficient to meet due process standards provided taxpayers are afforded meaningful backward-looking relief for taxes paid under a tax scheme subsequently found to be unconstitutional. *McKesson*, 496 U.S. at 22, 110 L. Ed. 2d at 27.

In *McKesson*, the petitioner challenged a Florida tax scheme which afforded special rate reductions for certain specified citrus, grape, and sugarcane products, all of which are commonly grown in Florida and used in alcoholic beverages produced in the state. The petitioner, a wholesale distributor of alcoholic beverages whose products did not qualify for the rate reduction, followed the statutory procedure for repayment or refund of taxes by paying the applicable taxes each month and then seeking a refund from the Florida Office of the Comptroller on the ground that the tax scheme unlawfully provided preferences for distributors of certain local products. Upon denial of its refund request, petitioner brought suit in a Florida trial court against the comptroller and the Florida Division of Alcoholic Beverages. The petitioner's suit challenged the constitutionality of the tax under both the Federal Constitution's Commerce Clause and other federal and state constitutional provisions. The petitioner requested declaratory and injunctive relief, and sought a refund of the excess taxes it had paid because of the tax scheme's discriminatory treatment. The trial court enjoined the state from giving effect to the preferences in

the future, but refused to provide a refund or any other relief to the petitioner for taxes it had already paid.

In affirming the trial court's order, the Florida Supreme Court held that while the preferential rate reductions should be given no future operative effect, the petitioner was not entitled to a refund of previously paid taxes. The court reasoned that the Division of Alcoholic Beverages and Tobacco had relied in good faith on a presumptively valid statute. Additionally the petitioner, if given a refund, would most likely receive a windfall, since the cost of the tax likely had been passed on to its customers.

The United States Supreme Court reversed, holding that postdeprivation remedies for unlawful taxes do not meet due process standards if a taxpayer who has paid the illegal tax meets the statutory requirements for a remedy, but is limited to prospective relief. *Id.* at 31, 110 L. Ed. 2d at 32. The Court held:

> If a State places a taxpayer under duress promptly to pay a tax when due and relegates him to a postpayment refund action in which he can challenge that tax's legality, the Due Process Clause of the Fourteenth Amendment obligates the State to provide meaningful backward-looking relief to rectify any unconstitutional deprivation.
>
> Florida requires taxpayers to raise their objections to the tax in a postdeprivation refund action. To satisfy the requirements of the Due Process Clause, therefore, in this refund action the State must provide taxpayers with, not only

> a fair opportunity to challenge the accuracy and legal validity of their tax obligation, but also a clear and certain remedy.

Id. at 38-39, 110 L. Ed. 2d at 37.

McKesson was a troubling case because Florida did not provide a full refund of the challenged tax even after the taxpayer complied with all of the procedural requirements for challenging the tax later determined to be unconstitutional. *McKesson* makes abundantly clear, as do the cases it cites, that a full refund of the challenged tax is all that due process requires provided that a fair opportunity to contest the tax is given. The Court said:

> The State may, of course, choose to erase the property deprivation itself by providing petitioner with a full refund of the tax payments.
>
> . . . .
>
> In the end, the State's postdeprivation procedure would provide petitioner with all of the process it is due: an opportunity to contest the validity of the tax and a "clear certain remedy" designed to render the opportunity meaningful by preventing any permanent unlawful deprivation of property.

Id. at 39-40, 110 L. Ed. 2d at 38. There can, of course, be no clearer or more certain remedy nor more meaningful backward-looking relief than a full refund of the challenged tax.

Plaintiffs contend, nevertheless, that the State cannot, consistent with due process, deprive them of full refunds of all

taxes paid in all tax years within the period of the statute of limitations even though these taxes were not duly challenged under the procedures established by section 105-267. Again, *McKesson* answers this contention adversely to plaintiffs' position.

McKesson holds that a state may provide full refunds to taxpayers, and at the same time, protect its fiscal stability by imposing "various procedural requirements on actions" seeking such refunds:

> The State might, for example, provide by statute that refunds will be available only to those taxpayers paying under protest or providing some timely notice of complaint; execute any refunds on a reasonable installment basis; enforce relatively short statutes of limitations applicable to such action . . . . The State's ability in the future to invoke such procedural protections suffices to secure the State's interest in stable fiscal planning when weighed against its constitutional obligation to provide relief for an unlawful tax.

Id. at 45, 110 L. Ed. 2d at 41. Indeed, in remanding the case to the Florida Supreme Court, the United States Supreme Court noted, "upon remand the State may invoke as an independent basis for refusing to provide a refund, petitioner's failure to comply with a notice requirement that was in effect at the time of petitioner's tax payments." *Id.* at 24 n.4, 110 L. Ed. 26 at 28 n.4.

North Carolina thus gives taxpayers desiring to challenge the illegality, or unconstitutionality, of a tax a clear and certain

remedy and meaningful, backward-looking relief by providing a full refund of the tax if the challenge is successful. It also provides a clear and fair opportunity to contest the tax by the procedures set out in section 105-267. Denial of refunds to taxpayers for the tax years for which they failed to comply with this procedure does not, as the Court made clear in *McKesson*, deprive these taxpayer of constitutional due process.[3]

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[3] A "state is free, of course, to provide broader relief as a matter of state law than is required by the Federal Constitution. *McKesson*, 496 U.S. at 52 n.36, 110 L. Ed. 2d at 45 n.36. The North Carolina General Assembly has chosen to do this by enacting N.C.G.S. § 105-151.20, which provides:

> A taxpayer who received government retirement benefits during the 1988 tax year may claim a credit against the tax imposed by this Division equal to the amount by which the tax under this Division paid by the taxpayer for the 1988 tax year would have been reduced if one of the taxpayer' s government retirement benefits had been included in the taxpayer's taxable income. If a taxpayer received a refund of any tax paid under this Division on government retirement benefits for the 1988 tax year, the amount of the refund reduces the amount of the credit allowed under this section . . . .
>
> The credits allowed under this section shall be taken in equal installments over the taxpayer's first three taxable years beginning on or after January 1, 1990. The credit allowed under this section may not exceed the amount of tax imposed by this Division reduced by the sum of all credits allowed against the tax except payments of the tax made by or on behalf of the taxpayer.

N.C.G.S. § 105-151.20 (1992). Thus federal retirees who were ineligible for tax refunds because of failure to comply with protest requirements were entitled to relief for the 1988 tax year in the form of tax credits.

Other jurisdictions reviewing taxpayers' eligibility for refunds of taxes paid pursuant to a statute subsequently pronounced unconstitutional, have applied the due process principles articulated in *McKesson* and, in several cases, have awarded or denied refunds to taxpayers on the basis of their compliance with state procedural refund requirements. *Jenkins v. Missouri*, 962 F.2d 762 (8th. Cir. 1992) (refund of unlawfully levied tax limited to those taxpayers who paid under protest), *cert. denied*, _____ U.S. _____, 121 L. Ed. 2d 242 (1992); *Farrar v. Franchise Tax Board*, 15 Cal. App. 4th 10, 18 Cal. Rptr. 26 611 (1993) (failure to provide timely notice of class claim warranted dismissal of claim for refunds), *cert. denied*, ___ U.S. ___, ___ L. Ed. 2d __, 62 USLW 3449, 62 USLW 3451 (Jan. 10, 1994); *Hagge v. Iowa Department of Revenue and Finance*; 504 N.W.2d 448 (Iowa 1993) (refund awarded to taxpayers who timely filed amended returns within the limitation period); *Ragsdale v. Department of Revenue*, 312 Or. 529, 823 P.2d 971 (1992) (statutes requiring taxpayer to file legal action before becoming eligible for refunds and denying taxpayer refunds for taxes collected prior to the filing of the action was a reasonable procedural barrier).

Plaintiffs contend that by its later decision in *Harper*, the United States Supreme Court somehow altered *McKesson*. Their argument seems to be that *Harper*, if not *McKesson*, requires a refund of the taxes paid in all tax years within the period of the statute of limitation even though the taxpayers failed to comply with the statutory procedures for challenging the tax for those years. We disagree. In our view, insofar as *Harper* addressed due process concerns with regard to statutes providing relief from unconstitutional taxes, it reaffirmed what was held and said in *McKesson*.

The issue in *Harper* was whether the Virginia Supreme Court had erred in not giving retroactive effect to *Davis*. The United States Supreme Court concluded that it had. *Harper* involved an action for refund of taxes unlawfully assessed for the years 1985 to 1988 in violation of *Davis*. In response to *Davis*, Virginia had repealed its exemption from state income taxation for state and local government employees. It also enacted a statute under which taxpayers could seek a refund of state taxes imposed on federal retirement benefits in the years 1985, 1986, 1987 and 1988 for up to one year from the date of the final determination as to whether Virginia must refund these taxes.

The petitioners in *Harper*, 421 federal civil service and military retirees in Virginia, sought refunds of the taxes improperly or erroneously assessed. The trial court denied the refunds on the ground that the *Davis* decision was to be applied prospectively. The Supreme Court of Virginia affirmed, concluding that because *Davis* was to be applied prospectively, the pre-Davis assessments were not improper under Virginia's tax refund statute.

The United States Supreme Court vacated the Virginia Supreme Court's decision and remanded the case in light of the Court's decision in *James B. Beam Distilling Co. v. Georgia*, 501 U.S. _____, 115 L. Ed. 2d 481 (1991), which held that an earlier decision invalidating excise taxes on alcoholic beverages was retroactively applicable to claims arising from facts predating the earlier decision. On remand, the Supreme Court of Virginia affirmed its prior decision in all respects on the ground that the issue of retroactivity was not decided in *Davis* because Michigan had not contested plaintiff's entitlement to a refund.

Reversing the Virginia Supreme Court, the United States Supreme Court held that *Davis* was to be applied retroactively. The Court noted, however, that retroactive application of *Davis* did not necessarily entitle the petitioners to a refund. Rather, Virginia was only required to provide relief consistent with federal due process. *Harper*, 509 U.S. at ____, 125 L. Ed. 2d at 88. The *Harper* Court did not fashion a new test for due process. Instead, it relied on well-established tests enunciated in *McKesson* and earlier cases. The Court said:

> Because we have decided that *Davis* applies retroactively to the tax years at issue in petitioners' refund action, we reverse the judgment below. We do not enter judgment for petitioners, however, because federal law does not necessarily entitle them to a refund. Rather, the Constitution requires Virginia "to provide relief consistent with federal due process principles." *American Trucking*, 496 U.S. at 181, 110 L. Ed. 2d 148, 110 S.Ct. 2323 (plurality opinion). Under the Due Process Clause, U.S. Const., Amdt. 14, § 1, "a State found to have imposed an impermissibly discriminatory tax retains flexibility in responding to this determination." *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 39-40, 110 L. Ed. 2d 17, 110 S.Ct. 2238 (1990). If Virginia "offers a meaningful opportunity for taxpayers to withhold contested tax assessments and to challenge their validity in a predeprivation hearing," the "availability of a predeprivation hearing constitutes a procedural safeguard sufficient by itself to satisfy the Due Process

> Clause." *Id.* at 38, n.21, 110 L. Ed. 26 17, 110 S.Ct. 2238. On the other hand, if no such predeprivation remedy exists, "the Due Process Clause of the Fourteenth Amendment obligates the State to provide meaningful backward-looking relief to rectify any unconstitutional deprivation." *Id.* at 31, 110 L. Ed. 2d 17, 110 S.Ct. 2238 (footnotes omitted). In providing such relief, a State may either award full refunds to those burdened by an unlawful tax or issue some other order that "create(s) in hindsight a nondiscriminatory scheme." *Id.* at 40, 110 L. Ed. 26 17, 110 S.Ct. 2238. *Cf. Davis*, 489 U.S: at 818, 103 L. Ed. 26 891, 109 S.Ct. 1500 (suggesting that a State's failure to respect intergovernmental tax immunity could be cured "either by extending [a discriminatory] tax exemption to retired federal employees . . . or by eliminating the exemption for retired state and local government employees").

Id. at ___, 125 L. Ed. 2d at 88-89.

The *Harper* Court also noted that were Virginia to have provided an adequate predeprivation remedy, that is, a "meaningful opportunity for taxpayers to withhold contested tax assessments and challenge their validity in a predeprivation hearing," due process would be satisfied. *Id.* at ___, 125 L. Ed. 2d at 89 (quoting *McKesson*, 496 U.S. at 38, 110 L. Ed. 2d at 37).

Where no such predeprivation remedy exists, "the Due Process Clause of the Fourteenth Amendment obligates the State to provide meaningful backward-looking relief to rectify

any unconstitutional deprivation." *Id.* (quoting *McKesson*, 496 U.S. at 31, 110 L. Ed. 2d at 32).

In its brief before the Supreme Court the State of Virginia argued that "[t]axpayers in Virginia are entitled to challenge a tax assessment in a prepayment procedure set forth in §§ 58.1-1821 and 58.1-1822 of the Virginia Code." Brief for Respondent at 47, *Harper v. Virginia Department of Taxation*, 509 U.S. _____, 125 L. Ed. 2d 74 (1993). Thus, Virginia contended petitioners "had a clear, meaningful, prepayment opportunity to challenge the validity of the tax of which they now complain." *Id.* The sufficiency of this predeprivation procedure had not been reviewed by the Virginia Supreme Court. The United States Supreme Court held:

> The constitutional sufficiency of any remedy thus turns (at least initially) on whether Virginia law "provide[s] a[n] [adequate] form of `predeprivation process,' for example, by authorizing taxpayers to bring suit to enjoin imposition of a tax prior to its payment, or by allowing taxpayers to withhold payment and then interpose their objections gas defenses in a tax enforcement proceeding." *McKesson*, 496 U.S. at 36-37, 110 L. Ed. 2d 17, 110 S.Ct 2238. Because this issue has not been properly presented, we leave to Virginia courts this question of state law and the performance of other tasks pertaining to the crafting of any appropriate remedy. Virginia is free to choose which form of relief it will provide, so long as that relief satisfies the minimum federal requirements we have outlined." *Id.* at 51-52, 110 L. Ed. 26 17, 110 S.Ct 2238.

Harper, 509 U.S. at ___, 125 L. Ed. 2d at 89. The constitutionality of a postdeprivation remedy, such as that afforded in North Carolina, was not before the Court in *Harper*. The Court chose to comment on, but did not decide, whether Virginia's predeprivation remedy satisfied due process.

Thus, *Harper* did not modify the Court's previous jurisprudence, including McKesson, regarding the tests for determining whether a state's postdeprivation remedy by which a tax may be challenged on legal or constitutional grounds satisfies due process. Rather, the *Harper* Court made it clear that a state satisfied due process if it offered taxpayers relief consistent with the due process standards delineated in McKesson.

III.

We next turn to plaintiffs' argument that any defenses by the State under section 105-267 to plaintiffs' federal challenges have been settled by res judicata and collateral estoppel. The basis of plaintiffs' argument is the denial of the State's motion to dismiss based on the Tax Injunction Act, 28 U.S.C. § 1341, in the companion case brought by plaintiffs in The United States District Court for the Eastern District of North Carolina, Raleigh Division. *Swanson v. Powers* (E.D.N.C. 1990) (No. 89-282-CIV-5-H). We find no merit in this argument because there has been no final adjudication of the federal case.

> Under *res judicata*, a final judgment on the merits in a prior action will prevent a second suit based on the same cause of action between the same parties or those in privity with them. When the plaintiff prevails, his cause of action is said to have "merged" with the judgment; where

> defendant prevails, the judgment "bars" the plaintiff from further litigation. In either situation, all matters, either fact or law, that were or should have been adjudicated in the prior action are deemed concluded. See Restatement (Second) of Judgments 18, 19 (1982); 1B Moore's Federal Practice 405[1] at 181-85 (2d ed. 1984).

Thomas M. McInnis & Assoc., Inc. v. Hall, 318 N.C. 421, 428, 349 S.E.2d 552, 556-57 (1986). For *res judicata* to apply, a party must show that a "previous suit has resulted in final judgment on the merits, that the same cause of action is involved, and that [plaintiffs] and [the State] were either parties or stand in privity with parties." *Id.* at 429, 349 S.E.2d at 557. Similarly,

> Under collateral estoppel as traditionally applied, a final judgment on the merits prevents relitigation of issues actually litigated and necessary to the outcome of the prior action in a later suit involving a different cause of action between the parties or their privies. See Restatement (Second) of Judgments § 27 (1982); 1B Moore's Federal Practice 0.441[1] at 718 (2d ed. 1984).

Id. (footnote omitted). Thus, collateral estoppel, like *res judicata*, only occurs "when there has been a final judgment or decree." *King v. Grindstaff*, 284 N.C. 348, 355, 200 S.E.2d 799, 805 (1973).

In the federal case, by an order dated 26 October 1993, United States District Judge Malcolm H. Howard found that "a

final judgment has not been issued in this case and . . . this court has never ordered that this case be closed"; and Judge Howard ruled "the court hereby puts all parties on notice that this case is not closed and the court stands ready to hear any and all matters that properly come before it." *Swanson v. Powers* (E.D.N.C. 1990) (No. 89-282-CIV-5-H). Because the requisite element of a final judgment is lacking, neither *res judicata* nor collateral estoppel based on the federal litigation apply.

For the foregoing reasons, the decision of the superior court granting summary judgment in favor of plaintiffs is reversed. The case is remanded for entry of judgment for defendants dismissing the action.

Reversed and remanded.

No. 64PA91 - Swanson, et al. v. State [Filed: March 4, 1994]

Justice MITCHELL dissenting.

Neither the defendants nor the majority of this Court dispute the fact that the defendants have unlawfully collected taxes from the plaintiffs through the application of an unconstitutionally discriminatory tax. The issue is whether the defendants must return the money they have unlawfully taken from the taxpayer-plaintiffs, or may keep that money because the plaintiffs have not sought to recover it in strict accordance with the requirements set forth in N.C.G.S. § 105-267. I believe that under the particular facts presented by this case, the plaintiffs have been denied due process of law. Therefore, I must dissent from the opinion of the majority which holds to the contrary and denies relief to the taxpayer-plaintiffs.

At the outset, I take exception to the apparent view of the majority that by failing to comply with the procedural prerequisites of N.C.G.S. § 105-267, the plaintiffs somehow voluntarily paid the unconstitutional taxes in question. When, as here, a tax is paid to avoid financial sanctions or a seizure of real or personal property, the tax is paid under duress. *McKesson v. Division of Alc. Bev.*, 496 U.S. 18, 39 n.21, 110 L Ed. 2d 17, 37 n.21 (1990).

> In contrast, if a State chooses not to secure payments under duress and instead offers a meaningful opportunity for taxpayers to withhold contested tax assessments and to challenge their validity in a predeprivation hearing, payments tendered may be deemed "voluntary." The availability of a predeprivation hearing constitutes a procedural safeguard against unlawful deprivation sufficient by itself to satisfy the Due Process Clause, and taxpayers cannot complain if they fail to avail themselves of this procedure.

Id. As the opinion of the majority concedes, North Carolina law did not provide the plaintiffs with any form of predeprivation remedy. Therefore, they may not be denied recovery on the basis of any ruling grounded in the motion that they have somehow voluntarily paid the unconstitutional taxes in question, thereby rendering those unlawfully collected taxes nonrefundable.

> When, as here, the State places a taxpayer under duress promptly to pay a tax when due and relegates him to a postpayment refund action in which he can challenge the tax's legality, the Due

> Process Clause of the Fourteenth Amendment obligates the State to provide meaningful backward-looking relief to rectify any unconstitutional deprivation.

Id. at 31, 110 L. Ed. 2d at 32 (footnotes omitted). "In providing such relief, a State may either award full refunds to those burdened by an unlawful tax or issue some other order that `create[s] in hindsight a nondiscriminatory scheme.'" *Harper v. Virginia Dept. of Taxation*, 509 U.S. _____, 125 L. Ed. 2d 74, 89 (1993) (quoting *McKesson*, 496 U.S. at 40, 110 L. Ed 2d at 38). Any such postdeprivation procedure provides all of the process due, if it provides "an opportunity to contest the validity of the tax and a `clear and certain remedy' designed to render the opportunity meaningful by preventing any permanent unlawful deprivation of property." *McKesson*, 496 U.S. it 40, 110 L. Ed. 2d at 38. I am convinced under the facts presented by the present case, however, that N.C.G.S. § 105-267 does not provide these plaintiffs the type of meaningful backward-looking relief required by the Due Process Clause.

The opinion of the majority concludes that the taxpayer-plaintiffs were required under N.C.G.S. § 105-267 to make a postdeprivation demand upon the administrative functionaries responsible for collecting the taxes in question and then wait the required period of time thereafter before initiating any court action seeking to recover money taken from them unlawfully pursuant to an unconstitutional tax. However, courts have uniformly held that plaintiffs will not be required to exhaust administrative remedies before bringing suit, where pursuing such administrative remedies would be futile. Pursuing an administrative remedy is "futile" when it is useless to do so either as a legal or practical matter. See *Honig v. Doe*, 484 U.S. 305, 327, 98 L. Ed. 2d 686, 709 (1988). For me, this clearly is

a case in which it would have been futile for the plaintiffs to exhaust their administrative remedies under N.C.G.S. § 105-267 before seeking relief in the courts.

In the present case, neither of the State functionaries who have been made defendants in this case -- the Secretary of Revenue and the State Treasurer -- have or have ever had the authority to grant the relief sought by the taxpayer-plaintiffs. Those defendants, who have administrative responsibilities with regard to the tax at issue, did not and do not have the power to pass upon the constitutionality of that tax, since decisions as to the constitutionality of tax statutes are *exclusively* for the judiciary. *Bailey v. State of North Carolina*, 330 N.C. 227, 246, 412 S.E.2d 295, 306 (1991), *cert. denied*, _____ U.S. _____ , 118 L. Ed. 2d 547 (1992). Thus, it is clear beyond question that the conclusion of the majority requiring these taxpayers to "jump through the procedural hoops adopted and applied by the State bureaucracy under N.C.G.S. § 105-267" amounts to a holding that they were entitled to relief only if they did an utterly vain and useless act. *Bailey*, 330 N.C. at 248-49, 412 S.E.2d at 308 (Mitchell, J., dissenting). That being the case, I reject the majority's view that the statute provides meaningful backward-looking relief of the sort which is adequate to satisfy minimum due process requirements. *See id.; Reich v. Collins*, 437 S.E.2d 320, 322-25 (Ga. 1993) (Carley, J., joined by Sears-Collins, J., dissenting). Therefore, I also reject the majority's conclusion that the defendants are entitled to the entry of a judgment dismissing the taxpayers' action against them.

Under the opinion of the majority, these taxpayer-plaintiffs would be entitled to a refund only if they had foreseen at an early stage that the tax in question was unconstitutional -- foresight which would have exceeded that of the legislature, the defendants who are experts in such matters, and this Court. *See*

Swanson v. State of North Carolina, 329 N.C. 576, 407 S.E.2d 791 (1991), vacated and remanded, ___ U.S. ___ 125 L. Ed. 2d 713 (1993) (in which a majority of this Court held that these plaintiffs were not entitled to refunds of the taxes in question because the decision of the Supreme Court of the United States in *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 103 L. Ed. 2d 891 (1989), declaring taxes such as that at issue here unconstitutional, did not apply retroactively). I am completely aware that a concern for the ability of taxing entities such as the various states and local governments to engage in sound fiscal planning has led to the adoption of rules which are heavily weighted against the taxpayers and in favor of the taxing entity in cases such as this. I believe, however, that the opinion of the majority in the present case goes well beyond any legitimate need supporting such concerns and upholds a sham procedure for postdeprivation relief which was futile from the outset in this case. Surely, this unseemly result may only be properly characterized as tilting the scales too far in favor of the taxing entity and denying these taxpayers fundamental due process.

For the foregoing reasons, I believe that the taxpayer-plaintiffs have been denied due process of law by the majority's interpretation and application of N.C.G.S. § 105-267. Therefore, I respectfully dissent. [Justice Parker joins in this dissenting opinion.]

APPENDIX F

LIST OF PARTIES TO THE PROCEEDING

Petitioners

Federal Pensioners--Class A

Norman W. Swanson
Henry F. Murray
Carl L. Whitney
William E. Nicholson, III
Charles A. Dancy
Melvin F. Eyerman
Ira N. Schwarz
John L. Powell, Jr.
Galina Elworth
Donald V. Wallace
William E. Denton
Robert A. Nisbet
Walter J. Bartnikowski
Ralph P. Hunt
Marion B. Zollicoffer
William H. Talbert
Billy Clark
Wallace M. Davis
Grady L. Strange
Hamilton M. Howe
Mary L. Pritchard
Robert B. Campbell
Browning Adams
Pritchard G. Adams
William H. Adams
Edward H. Allen
Flossie P. Allen
Joseph A. Allen
Rachel C. Allred
Helen L. Anctil
Leo I. Anctil
Ronald E. Anderson
Clarence P. Armstrong
Carroll W. Austin
F. L. Austin, Jr.
Donald P. Bahr
Paul Ballus
Charles D. Barker, Sr.
Walter E. Barkhouse
Edward C. Barret
James L. Baxter
Russell W. Beard
Bernard L. Beatty
Richard K. Bell
Leo E. Benade
Sherman W. Betts
Joseph H. Betz
Robert L. Blevins
Dranklin M. Blunt
Timothy C. Bolick

Margaret C. Boone
Henry A. Botkin
Alex Bourdas
Ola May (Tate) Bovender
Eugene A. Bowen
Lavaune K. Breda
Marlowe G. Breda
Trond G. Brekke
Laura B. Brendle
Millard Bridgers
Clarence M. Bridges
Doris K. Bridges
Cyrus H. Brooks, Jr.
Daniel R. Brown
K. A. Brown
William D. Brown
Betty P. Bullock
Robert S. Bullock
Findley Burns, Jr.
Ray G. Burrell
Richard E. Bush
James M. Byrne
Norman L. Carlton
Matthew E. Carmean
Frank Cates
J. Crawford Caton
Harry E. Chamberlain
Vincent H. Chase
Paul F. Chavez
Woodrow H. Childress
John G. Church
Herman L. Clanton
Robert L. Clarke
Charles C. Clausen, Sr.
Dennis E. Cleckner
Steve P. Clemenic
Lacy W. Coates
Rucia A. Cobb
James A. Coddington
Catheryn S. Coley
Laura K. Conder
James C. Conine
Marshall G. Cooper
Asbury Coward, III
Newton P. Cox
Ruth A. Cox
Burnette E. Creasman
Thomas J. Culkin
Hazel B. Curlee
Milton L. Dail
Beatrice G. Davis
Bernley S. Davis
Donald M. Davis
Essie M. Davis
George E. Davis
Robert J. Davis
Clifford H. Dawson
Calvin F. Dean
Orien G. Dean, Jr.
Jack M. Deaton
Violet B. Deitmaring
Arlen J. Devito
John E. Devlyn
Sara E. Devlyn
Joy E. Dickinson
Mrs. Leroy B. Dickinson
James E. Diffee
Delbert R. Dillon

Margaret H. Dopf
Raymond E. Dopf
Leroy M. Duffy
Charles F. Dupont
Bobby R. Eason
David Edmisten
Carl L. Effler
John H. Elder, Jr.
John R. Ellis
Manford G. Farr
Rita Festo
John J. Filan
Angelo A. Florentino
Robert W. Folden
Oscar F. Fowler
Melvin W. Fritz
Walton E. Fulcher
Robert C. Fuller
Walter E. Fuller
Frank W. Furches
Norman Carl Gaddis
Marshall L. Gaddy
Thomas B. Gardiner
Robert F. Geissler
William E. Gentner, Jr.
Thomas P. Ginn
Robert W. Goodman
John R. Gordon
Bernice C. Grandy, Jr.
Steven W. Grandy
Robert J. Green
Michael R. Greeson
James H. Griffin
Thomas M. Groome, Jr.
James W. Gross
Arthur S. Gunderson
Hert L. Hancock, Jr.
James M. Hardin
C. Lee Harris
Howard W. Harris
Paul H. Harvey
Roland R. Hatcher
Henry S. Heffley, Jr.
Carroll A. Hefner
Clarence J. Hensley, Jr.
Richard M. Heriot
Doris T. Herring
Novis S. Herring
Virginia R. Hildebrand
Mozelle L. Hinshaw
Herman J. Hipps
Rufus M. Hodgin
Donald R. Hoffman
Charles K. Hoffmeyer
Mary R. Holland
Edgar P. Holt
Ray Homesley
Ned A. Hood
Robert H. Hood
Stephen W. Hopkins
Clyde L. Howard, Jr.
Kevin G. Huges
Harvey R. Hurst
Sam P. Hyatt
John L. Irby
Mattie B. Ives
Francis Jacobs
Richard L. Jarrett

Jacqueline M. Jennings
Woodrow W. Jones
Donald L. Jorgenson
Kenneth R. Joseph
Patsie W. Joseph
Everette R. Keller
Bernard J. Kelley
Wilson P. Lemp
Howard Lee Kerr
Margaret C. Kerr
William S. Ketner
David L. G. King
Thomas M. King, Jr.
Evelyn W. Kinney
John E. Kirk
Paul E. Kirkland, Sr.
Raymond B. Kleber
George M. Knobl, Jr.
William F. Knopf
Max V. Krebs
William J. Kuhn, Jr.
James M. Langston, Jr.
Jane W. Langston
Elmer L. Lashua
John L. Latham
Daniel M. Lauderback
August R. Lawrence
Freida H. Lewis
Norwood P. Lewis
Henry G. Liles
Dorothy J. Liles
Walter E. Linthicum
Phyllis V. Lippard
George Lott
Robert P. Lucas
Allen M. Mabe
Thomas S. Maceluch
William F. Marcuson, Jr.
Warner G. Maupin
Lylton E. Maxwell
Oliver A. Mays
Andrew G. Mayse
Samuel S. McCachren
Elizabeth S. McCaskill
Elizabeth G. McDonald
Clyde W. McKirk
Donald D. McGuire
Norman H. McLaughlin
Doy W. McPhail
William Ray Medlin, Jr.
Ernest E. Miller
Margaret H. Miller
Edgar N. Millington
Harold J. Mitchener
Eugene E. Moody
Dorothy C. Moore
James C. Moore, Jr.
Lucie E. Moorman
Robert M. Moose
Jack B. Morris
Regena E. Morrison
Stanley B. Morse
Woodford T. Moseley
George R. Muse
R. J. Nettles
Thomas G. Newport
John E. Nitsche
Alfred P. Norwood

Johnnie M. Ochoa
Elvin E. Oglesby
Oliver G. Oja
Russell E. Olson
Lloyd A. Osborne
Paul B. Osgood
William C. Page
Lee R. Paramore
Lewis W. Pate
Charles R. Patton
Vernon J. Peebles
W. W. Pegues
Mary E. Penn
John D. Penn
Elliotte T. Perkins, Jr.
William H. Perry, Jr.
Paul J. Phillippi
Richard L. Phillips
Ruby A. Phillips
Frank J. Piazza, Sr.
Dallas Pickard, Jr.
George A. Pinter
Edward W. Piper
Frederick H. Pless
R. F. Hoke Pollock, Jr.
Lewington S. Ponder
Elbert Y. Poole
Jennette C. Poole
Martha Boyce Poteat
Edwin H. Price
Charles R. Pugh
Daniel J. Quesenberry
Milton H. Quinn
Louise M. Rabbino
Thomas M. Ramsey
Jack G. Ray
Marshall G. Ray
Hazel S. Redmon
George R. Reinhart, III
Annie E. Renkel
Madge O. Reynolds
Franklin E. Richardson, Jr.
Allen W. Rigsby
George M. Roberts
Jennings B. Robinson
James P. Roth
Phifer P. Rothman
Harold E. Ruble
Hilda H. Rultenberg
Donald E. Russell
George W. Sabo
Lyle E. Samson
Robert L. Scheer
Frederick L. Schuerman, Sr.
Robert J. Schullery
Elwood M. Shaulis
Robert T. Sheridan
Stanley T. Shipley
Charles B. Shivley
Charles A. Shue, Jr.
Ruth M. Shue
Elsie N. Simmons
Frederick E. Simmons
Mary B. Simpson
Manuel F. Siverio
Joseph A. Sizoo
Evelyn S. Smith

George B. Smith
James A. Smith
James E. Smith
James P. Smith
Joe F. Smith
Percy H. Smith
Joseph L. Sommer
Ray H. Spangler
James A. Sprankle
Wiley L. Standifer, Jr.
James W. Starbuck
Gertrude D. Starling
Stacy J. Starling
Henry C. Steed, Jr.
Roy C. Steeley
Arthur L. Stewart
Burlena J. Stewart
John R. Stewart, Jr.
George W. Stillway
Rita M. Stillway
Harold E. Stone
Clyde Dalton Stowe
Harry H. Strunk
E. C. Stumpf
Thomas A. Summey, Jr.
Ellis G. Sumner
Leo B. Sumner
Mildred Y. Sumner
Margaret K. Swink
James E. Sykes
Oliver B. Talbert
James D. Terrell
Clyde E. Thompson
Emogene M. Thompson
Fred L. Tracy
Rocco H. Trombello
John G. Truitt, Jr.
William H. Turk
James T. Vance
Frances A. Vanden
George W. Vanden
Ethel D. Vanhorn
Edward J. Vaughn
Edward Venkler
Roy L. Vick, Sr.
Kermit J. Vinson
Myrtle H. Vinson
William E. Wade
Floyd H. Waldrop
Wanda E. Wallace
Roland J. Weber
Grace F. Weiner
Lona C. Weisner
Lawrence O. Welch
Paul B. Welch, Jr.
George L. Westerlind
William B. White
T. M. Whittington, Jr.
George W. Wilkins
Robert S. Williams, Jr.
William C. Williams
Winton H. Williams
Harold P. Williamson
Edna Mae Wilson
Robert Graves Wilson, Jr.
Ernest G. Winstead
Peter S. Wondolowski
Robert V. Wood

Maynard B. Woodbury
Evelyn W. Woodbury
Jack R. Worley
John T. Worrell
George T. Worrell
George E. Yale, Jr.
William P. Yarborough

Respondent

Janice Faulkner, Secretary of Revenue of the State of North Carolina
North Carolina Department of Revenue, Harlan Boyles, Treasurer of the State of North Carolina

Federal Military Personnel-Class B

Charles L. Berry
Milton S. Price
Robert D. Lennon
Martin L. Dpeicher
Zebulon V. Moseley, III
Paul H. Turney
Gary W. O'Neal

APPENDIX G

North Carolina General Statute § 105-267 provides:

> No court of this State shall entertain a suit of any kind brought for the purpose of preventing the collection of any tax imposed in this Subchapter. Whenever a person shall have a valid defense to the enforcement of the collection of a tax assessed or charged against him or his property, such person shall pay such tax to the proper officer, and such payment shall be without prejudice to any defense of rights he may have in the premises. At any time within 30 days after payment, the taxpayer may demand a refund of the tax paid in writing from the Secretary of Revenue and if the same shall not be refunded within 90 days thereafter, may sue the Secretary of Revenue in the courts of the State for the amount so demanded. Such suit may be brought in the Superior Court of Wake County, or in the county in which the taxpayer resides at any time within three years after the expiration of the 90-day period allowed for making the refund. If upon the trial it shall be determined that such a tax or any part thereof was levied or assessed for an illegal or unauthorized purpose, or was for any reason invalid or excessive, judgment shall be rendered therefor, with interest, and the same shall be collected as in other cases. The amount of taxes for which judgment shall be

be refunded by the State; provided, nothing in this section shall be construed to conflict with or supersede the provisions of N.C. Gen. Stat. § 105-241.2. (1939, c. 158, s. 936; 1955, c. 1350, s. 15; 1957, c. 1340, s. 10; 1977, c. 946, s. 1.)

North Carolina General Statute **§ 105-266.1** provides:

(a) Any taxpayer may apply to the Secretary of Revenue for refund of tax or additional tax paid by him at any time within three years after the date set by the statute for the filing of the return or application for a license or within six months from the date of payment of such tax or additional tax, whichever is later. The Secretary shall grant a hearing thereon, and if upon such hearing he shall determine that the tax is excessive or incorrect he shall resettle the same according to the law and the facts, and adjust the computation of tax accordingly. The Secretary shall notify the taxpayer of his determination, and shall refund to the taxpayer the amount, if any, paid in excess of the tax found by him to be due; except that there shall be no refund to the taxpayer of any sum set off under the provisions of Chapter 105A, the Setoff Debt Collection Act.

* * *

(e) Nothing in this section shall be construed to conflict with or supersede the provisions of G.S. 105-241.2, and, with respect to tax paid to the Secretary of Revenue, the rights granted by this section are in addition to the rights provided by G.S. 105-267. (1957, c. 1340, s. 10; 1969, c. 44, s. 66; c. 1132, s. 2; 1973, c. 476, s. 193; 1979, c. 801, s. 91; 1981 (Reg. Sess., 1982), c. 1211, s. 2; 1987, c. 827, s. 22.)